ESSA Bancorp, Inc.
Form 10-K
December 11, 2009

SECURITIES AND EXCHANGE COMMISSION

100 F Street NE

Washington, D.C. 20549

FORM 10-K

x **Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the Fiscal Year Ended September 30, 2009

or

¨ **Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the transition period from ______ to ______

Commission File No. 001-33384

ESSA Bancorp, Inc.

(Exact name of registrant as specified in its charter)

Pennsylvania	**20-8023072**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification Number)**
200 Palmer Street, Stroudsburg, Pennsylvania	**18360**
(Address of Principal Executive Offices)	**Zip Code**

(570) 421-0531

(Registrant s telephone number)

Securities Registered Pursuant to Section 12(b) of the Act:

Title of each class	**Name of each exchange on which registered**
Common Stock, $0.01 par value	The NASDAQ Stock Market, LLC

Securities Registered Pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. YES ¨ NO x

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. YES ¨ NO x

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding twelve months (or for such shorter period that the Registrant was required to file such reports) and (2) has been subject to such requirements for the past 90 days. YES x NO ¨.

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES x NO ¨.

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of Registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ¨ .

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer	¨	Accelerated filer	x
Non-accelerated filer	¨	Smaller reporting company	¨

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). YES ¨ NO x

As of December 8, 2009, there were 16,980,900 shares issued and 14,595,320 shares outstanding of the Registrant s Common Stock.

The aggregate market value of the voting and non-voting common equity held by non-affiliates of the Registrant, computed by reference to the last sale price on December 8, 2009, was $153,839,716.

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DOCUMENTS INCORPORATED BY REFERENCE

1. Proxy Statement for the 2010 Annual Meeting of Stockholders of the Registrant (Part III).

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PART I

Item 1. Business
Forward Looking Statements

This Annual Report contains certain forward-looking statements which may be identified by the use of words such as believe, expect, anticipate, should, planned, estimated and potential. Examples of forward-looking statements include, but are not limited to, estimates with respect to our financial condition, results of operations and business that are subject to various factors which could cause actual results to differ materially from these estimates and most other statements that are not historical in nature. These factors include, but are not limited to, general and local economic conditions, changes in interest rates, deposit flows, demand for mortgage, and other loans, real estate values, competition, changes in accounting principles, policies, or guidelines, changes in legislation or regulation, and other economic, competitive, governmental, regulatory, and technological factors affecting our operations, pricing products and services.

ESSA Bancorp, Inc.

ESSA Bancorp, Inc. is the Pennsylvania-chartered stock holding company of ESSA Bank & Trust. ESSA Bancorp, Inc. owns 100% of the outstanding shares of common stock of ESSA Bank & Trust. Since being formed in 2006, ESSA Bancorp, Inc. has engaged primarily in the business of holding the common stock of ESSA Bank & Trust. Our executive offices are located at 200 Palmer Street, Stroudsburg, Pennsylvania 18360. Our telephone number at this address is (570) 421-0531. ESSA Bancorp, Inc. is subject to comprehensive regulation and examination by the Office of Thrift Supervision. At September 30, 2009, ESSA Bancorp, Inc. had consolidated assets of $1.04 billion, consolidated deposits of $408.9 million and consolidated stockholders equity of $185.5 million. Its consolidated net income for the fiscal year ended September 30, 2009 was $6.6 million.

On April 3, 2007, ESSA Bancorp, Inc. consummated its stock offering, resulting in gross proceeds of $158.7 million, through the sale of 15,870,000 shares at a price of $10.00 per share. ESSA Bancorp, Inc. also contributed 1,110,900 shares of its common stock to the ESSA Bank & Trust Foundation along with $1.6 million in cash. Expenses related to the offering were approximately $2.9 million, which resulted in net proceeds of approximately $155.8 million prior to the contribution to the ESSA Bank & Trust Foundation.

ESSA Bancorp, Inc. loaned approximately $13.6 million to the ESSA Bank & Trust s Employee Stock Ownership Plan. ESSA Bancorp, Inc. retained approximately $64.3 million of the net proceeds of the offering prior to the contribution to the ESSA Bank & Trust Foundation, and the remainder of the net proceeds were contributed to ESSA Bank & Trust.

ESSA Bank & Trust

General

ESSA Bank & Trust was organized in 1916. ESSA Bank & Trust is a Pennsylvania chartered full-service, community-oriented savings association. We provide financial services to individuals, families and businesses through our thirteen full-service banking offices, located in Monroe and Northampton Counties, Pennsylvania. ESSA Bank & Trust is subject to comprehensive regulation and examination by the Pennsylvania Department of Banking and the Office of Thrift Supervision.

ESSA Bank & Trust s business consists primarily of accepting deposits from the general public and investing those deposits, together with funds generated from operations and borrowings, in residential first mortgage loans (including construction mortgage loans), commercial real estate loans, home equity loans and lines of credit, commercial and consumer loans. We offer a variety of deposit accounts, including checking, savings and certificates of deposits. We also offer asset management and trust services. We offer investment services through our relationship with PRIMEVEST Financial Services, Inc., a third party broker/dealer and investment advisor.

ESSA Bank & Trust s executive offices are located at 200 Palmer Street, Stroudsburg, Pennsylvania 18360. Our telephone number at this address is (570) 421-0531. Our website address is www.essabank.com.

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The Company is a public company, and files interim, quarterly and annual reports with the Securities and Exchange Commission (SEC). All filed SEC reports and interim filings can be obtained from the Bank s website, on the Investor Relations page, without charge from the Company.

Market Area

At September 30, 2009, our thirteen full-service banking offices consisted of twelve offices in Monroe County and one office in Northampton County, Pennsylvania. Our primary market for deposits is currently concentrated around the areas where our full-service banking offices are located. Our primary lending area consists of the counties where our branch offices are located, and to a lesser extent, the contiguous counties in the Commonwealth of Pennsylvania.

Monroe County is located in eastern Pennsylvania, situated 90 miles north of Philadelphia, 75 miles west of New York and 116 miles northeast of Harrisburg. Monroe County is comprised of 611 square miles of mostly rural terrain. Monroe County is the second-fastest growing county in Pennsylvania. Major industries include tourism, construction and educational facilities. Northampton County is located south of Monroe County and directly borders New Jersey. As of June 30, 2009, we had a deposit market share of approximately 19.7% in Monroe County, which represented the second largest deposit market share in Monroe County and less than 1.0% in Northampton County.

Lending Activities

Historically, our principal lending activity has been the origination of first mortgage loans for the purchase, construction or refinancing of one- to four-family residential real property. During the past five years, we have increased our originations of commercial real estate loans in an effort to increase interest income, diversify our loan portfolio, and better serve the community. These loans have increased from 7.2% of our total loan portfolio at September 30, 2005 to $68.0 million, or 9.2% of our total loan portfolio at September 30, 2009. One- to four-family residential real estate mortgage loans represented $603.8 million, or 81.7%, of our loan portfolio at September 30, 2009. Home equity loans and lines of credit totaled $46.8 million, or 6.3% of our loan portfolio at September 30, 2009. Commercial loans totaled $16.5 million, or 2.2% of our loan portfolio at September 30, 2009 and construction first mortgage loans totaled $1.7 million, or 0.2% of the total loan portfolio at September 30, 2009. We originate other consumer loans on a limited basis.

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Loan Portfolio Composition. The following table sets forth the composition of our loan portfolio, by type of loan at the dates indicated, excluding loans held for sale.

	At September 30,									
	2009		2008		2007		2006		2005	
	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent
	(Dollars in thousands)									
Residential first mortgage loans:										
One- to four-family	$ 603,830	81.7%	$ 572,038	80.3%	$ 500,104	80.0%	$ 452,406	80.4%	$ 421,169	81.7%
Construction	1,707	0.2	8,254	1.1	7,800	1.3	5,943	1.1	7,597	1.5
Commercial	16,452	2.2	11,987	1.7	7,699	1.2	6,159	1.1	5,310	1.0
Commercial real estate	68,040	9.2	69,505	9.8	58,447	9.3	47,479	8.4	36,984	7.2
Home equity loans and lines of credit	46,792	6.3	47,508	6.7	47,544	7.6	46,796	8.3	40,342	7.8
Other	2,526	0.4	3,059	0.4	3,875	0.6	4,247	0.7	4,204	0.8
Total loans receivable	$ 739,347	100.0%	$ 712,351	100.0%	$ 625,469	100.0%	$ 563,030	100.0%	$ 515,606	100.0%
Deferred loan costs (fees)	48		(546)		(1,418)		(2,498)		(3,062)	
Allowance for loan losses	(5,815)		(4,915)		(4,206)		(3,855)		(3,563)	
Total loans receivable, net	$ 733,580		$ 706,890		$ 619,845		$ 556,677		$ 508,981	

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Loan Portfolio Maturities and Yields. The following table summarizes the scheduled repayments of our loan portfolio at September 30, 2009. Demand loans, loans having no stated repayment schedule or maturity, and overdraft loans are reported as being due in one year or less.

	One- to Four-Family		Construction		Commercial		Commercial Real Estate	
	Amount	Weighted Average Rate	Amount	Weighted Average Rate	Amount	Weighted Average Rate	Amount	Weighted Average Rate
				(Dollars in thousands)				
Due During the Years Ending September 30,								
2010	$ 94	6.85%	$		$ 3,607	4.29%	$ 5,220	6.36%
2011	680	5.88%			215	7.45%	1,602	6.51%
2012	651	6.52%			943	7.19%	1,638	6.42%
2013 to 2014	8,290	5.11%			1,000	6.89%	7,503	6.46%
2015 to 2019	85,399	5.08%			3,421	4.52%	34,919	6.40%
2020 to 2024	130,326	5.22%			2,266	5.23%	3,455	6.27%
2024 and beyond	378,390	5.92%	1,707	5.22%	5,000	4.55%	13,703	5.77%
Total	$ 603,830	5.64%	$ 1,707	5.22%	$ 16,452	4.91%	$ 68,040	6.27%

	Home Equity Loans and Lines of Credit		Other		Total	
	Amount	Weighted Average Rate	Amount	Weighted Average Rate	Amount	Weighted Average Rate
			(Dollars in thousands)			
Due During the Years Ending September 30,						
2010	$ 524	6.62%	$ 833	6.83%	$ 10,278	5.69%
2011	273	6.58%	229	8.90%	2,999	6.63%
2012	578	6.69%	328	9.01%	4,138	6.85%
2013 to 2014	2,101	5.79%	1,014	7.66%	19,908	5.91%
2015 to 2019	8,657	6.31%	122	7.98%	132,518	5.50%
2020 to 2024	19,899	5.55%			155,946	5.29%
2024 and beyond	14,760	3.30%			413,560	5.80%
Total	$ 46,792	5.02%	$ 2,526	7.69%	$ 739,347	5.65%

The following table sets forth the scheduled repayments of fixed- and adjustable-rate loans at September 30, 2009 that are contractually due after September 30, 2010.

	Due After September 30, 2010		
	Fixed	Adjustable	Total
		(In thousands)	
Residential first mortgage loans:			
One- to four-family	$ 539,849	$ 63,887	$ 603,736
Construction	1,694	13	1,707
Commercial	11,292	1,553	12,845
Commercial real estate	29,569	33,251	62,820
Home equity loans and lines of credit	25,778	20,490	46,268
Other	1,693		1,693

Total	$ 609,875	$ 119,194	$ 729,069

Loan Originations and Repayments. Historically, we have originated residential mortgage loans pursuant to underwriting standards that generally conform to Fannie Mae and Freddie Mac guidelines. Loan origination activities are primarily concentrated in Monroe and Northampton Counties, Pennsylvania and secondarily from other Pennsylvania counties contiguous to Monroe County. New loans are generated primarily from the efforts of employees and advertising, a network of select mortgage brokers, other parties with whom we do business, customer referrals, and from walk-in customers. Loan applications are underwritten and processed at our corporate center.

One- to Four-Family Residential Loans. Historically, our primary lending activity has consisted of the origination of one- to four-family residential mortgage loans secured primarily by properties located in Monroe and

Northampton Counties, Pennsylvania. At September 30, 2009, approximately $603.8 million, or 81.7% of our loan portfolio, consisted of one- to four-family residential loans. Our origination of one- to four-family loans increased in fiscal year 2009 compared to fiscal years 2008 and 2007. Originations in fiscal year 2009 were positively influenced by a significant amount of refinancing activity due to record low mortgage rates. Generally, one- to four-family residential mortgage loans are originated in amounts up to 80% of the lesser of the appraised value or purchase price of the property, although loans may be made with higher loan-to-value ratios at a higher interest rate to compensate for the risk. Private mortgage insurance is generally required on loans with a loan-to-value ratio in excess of 80%. Fixed-rate loans are originated for terms of 10, 15, 20 and 30 years. At September 30, 2009, our largest loan secured by one- to four-family real estate had a principal balance of approximately $804,000 and was secured by a single family house. This loan was performing in accordance with its repayment terms.

We also offer adjustable-rate mortgage loans which have fixed terms of one, three, five or ten-years before converting to an annual adjustment schedule based on changes in a designated United States Treasury index. We originated $5.0 million of adjustable rate one- to four-family residential loans during the year ended September 30, 2009 and $12.3 million during the year ended September 30, 2008. Our adjustable rate mortgage loans provide for maximum rate adjustments of 200 basis points per adjustment, with a lifetime maximum adjustment of 500 basis points. Our adjustable rate mortgage loans amortize over terms of up to 30 years.

Adjustable rate mortgage loans decrease the risk associated with changes in market interest rates by periodically repricing, but involve other risks because, as interest rates increase, the principal and interest payments on the loan increase, thus increasing the potential for default by the borrower. At the same time, the marketability of the underlying collateral may be adversely affected by higher interest rates. Upward adjustment of the contractual interest rate is also limited by the maximum periodic and lifetime interest rate adjustments, permitted by our loan documents; and therefore, is potentially limited in effectiveness during periods of rapidly rising interest rates. At September 30, 2009, $63.9 million, or 10.6%, of our one- to four-family residential loans had adjustable rates of interest.

All one- to four-family residential mortgage loans that we originate include due-on-sale clauses, which give us the right to declare a loan immediately due and payable in the event that, among other things, the borrower sells or otherwise disposes of the real property subject to the mortgage and the loan is not repaid.

Regulations limit the amount that a savings bank may lend relative to the appraised value of the real estate securing the loan, as determined by an appraisal of the property at the time the loan is originated. For all purchase money loans, we utilize outside independent appraisers approved by the Board of Directors. All purchase money borrowers are required to obtain title insurance. Certain modest refinance requests may utilize an automated valuation model and title search. We also require fire and casualty insurance and, where circumstances warrant, flood insurance.

Home Equity Loans and Lines of Credit. Home equity loans and lines of credit are generated almost exclusively by our branch staff. Eligible properties include primary and vacation homes in northeastern Pennsylvania, with the large majority of loans being originated in Monroe County. As of September 30, 2009, home equity loans and lines totaled about $46.8 million, or 6.3% or our loan portfolio.

The maximum combined loan-to-value originated is currently 70-80%, depending on the collateral and the holder of the first mortgage. There is a modest portion of the portfolio originated in years past that contains original combined loan-to-values of up to 90%. Our home equity lines of credit typically feature a 10 year draw period with interest-only payments permitted, followed by another 10 years of fully amortizing payments with no further ability to draw funds. Similar combined loan-to-value characteristics and standards exist for the lines as are outlined above for the loans.

Loan underwriting standards restrict the size of a junior lien loan to $200,000. All loans exceeding 70-75% of value require an appraisal by bank-approved, licensed appraisers. Loans with lesser loan-to-value ratios may have utilized either automated valuation models or county tax assessments. Title/lien searches are secured on all home equity loans and lines greater than $25,000.

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Commercial Real Estate Loans. At September 30, 2009, $68.0 million, or 9.2% of our total loan portfolio consisted of commercial real estate loans. Commercial real estate loans are secured by office buildings, mixed-use properties and other commercial properties. We generally originate adjustable rate commercial real estate loans with an initial term of five years and a repricing option, and a maximum term of up to 25 years. The maximum loan-to-value ratio of our commercial real estate loans is 85%. At September 30, 2009, we had 269 commercial real estate loans with an outstanding balance of $68.0 million. At September 30, 2009, our largest commercial real estate loan balance was $2.6 million, which was performing in accordance with its terms. At September 30, 2009, four of our loans secured by commercial real estate totaling $580,000 were not performing in accordance with their terms and were on nonaccrual status.

We consider a number of factors in originating commercial real estate loans. We evaluate the qualifications and financial condition of the borrower, including credit history, profitability and expertise, as well as the value and condition of the mortgaged property securing the loan. When evaluating the qualifications of the borrower, we consider the financial resources of the borrower, the borrower s experience in owning or managing similar property and the borrower s payment history with us and other financial institutions. In evaluating the property securing the loan, the factors we consider include the net operating income of the mortgaged property before debt service and depreciation, the ratio of the loan amount to the appraised value of the mortgaged property and the debt service coverage ratio (the ratio of net operating income to debt service) to ensure that it is at least 120% of the monthly debt service. All commercial real estate loans in excess of $250,000 are appraised by outside independent appraisers approved by the Board of Directors. Personal guarantees are obtained from commercial real estate borrowers although we will occasionally consider waiving this requirement based upon the loan-to-value ratio of the proposed loan. All purchase money and asset refinance borrowers are required to obtain title insurance. We also require fire and casualty insurance and, where circumstances warrant, flood insurance.

Loans secured by commercial real estate generally are considered to present greater risk than one- to four-family residential loans. Commercial real estate loans often involve large loan balances to single borrowers or groups of related borrowers. Repayment of these loans depends to a large degree on the results of operations and management of the properties securing the loans or the businesses conducted on such property, and may be affected to a greater extent by adverse conditions in the real estate market or the economy in general. Accordingly, the nature of these loans makes them more difficult for management to monitor and evaluate.

First Mortgage Construction Loans. At September 30, 2009, $1.7 million, or 0.2%, of our total loan portfolio consisted of first mortgage construction loans. Most of our first mortgage construction loans are for the construction of residential properties. We currently offer fixed and adjustable-rate residential first mortgage construction loans. First mortgage construction loans are generally structured for permanent mortgage financing once the construction is completed. At September 30, 2009, our largest first mortgage construction loan balance was $391,000. The loan was performing in accordance with its terms. First mortgage construction loans, once converted to permanent financing, generally repay over a thirty-year period. First mortgage construction loans require only the payment of interest during the construction period. First mortgage construction loans will generally be made in amounts of up to 80% of the appraised value of the completed property, or the actual cost of the improvements. Funds are disbursed based on our inspections in accordance with a schedule reflecting the completion of portions of the project.

First mortgage construction loans generally involve a greater degree of credit risk than one- to four-family residential mortgage loans. The risk of loss on a construction loan depends upon the accuracy of the initial estimate of the value of the property at completion of construction compared to the estimated cost of construction.

For all loans, we utilize outside independent appraisers approved by the Board of Directors. All borrowers are required to obtain title insurance. We also require fire and casualty insurance and, where circumstances warrant, flood insurance on properties.

Other Loans. We offer a variety of loans that are either unsecured or secured by property other than real estate. These loans include loans secured by deposits, personal loans and automobile loans. At September 30, 2009, these other loans totaled $2.5 million, or 0.4% of the total loan portfolio.

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Loan Approval Procedures and Authority. The loan approval process is intended to assess the borrower s ability to repay the loan, the viability of the loan, and the adequacy of the value of the property that will secure the loan. To assess the borrower s ability to repay, we review each borrower s employment and credit history and information on the historical and projected income and expenses of mortgagors. All residential mortgage loans in excess of the conforming loan limit but not more than $500,000 must be approved by one of the following: President or Chief Lending Officer. All loans in excess of $500,000 but not more than $750,000 must be approved by any two of the following: President, Chief Lending Officer and the Vice President, Branch Administration. All loans in excess of $750,000 to $1.25 million must be approved by the Management Loan Committee. The Management Loan Committee consists of the President, Chief Lending Officer, Vice President, Branch Administration and Vice President, Commercial Lending. All loans in excess of $1.25 million must be approved by the Board of Directors.

Non-Performing Loans and Problem Assets

After a real estate secured loan becomes 15 days late, we deliver a computer generated late charge notice to the borrower and will attempt to contact the borrower by telephone. When a loan becomes 30 days delinquent, we send a delinquency letter to the borrower. We then attempt to make satisfactory arrangements to bring the account current, including interviewing the borrower, until the mortgage is brought current or a determination is made to recommend foreclosure, deed-in-lieu of foreclosure or other appropriate action. After 60 days, we will generally refer the matter to the Board of Directors who may authorize legal counsel to commence foreclosure proceedings.

Mortgage loans are reviewed on a regular basis and such loans are placed on non-accrual status when they become more than 90 days delinquent. When loans are placed on non-accrual status, unpaid accrued interest is fully reserved, and further income is recognized only to the extent received.

Non-performing Loans. At September 30, 2009, $5.2 million (or less than 1.0% of our total loans) were non-performing loans. The majority of these loans, or $3.8 million, were residential first mortgage loans that were 90 days or more past due or troubled debt restructured loans that were considered non-performing at September 30, 2009.

Real Estate Owned. At September 30, 2009, the Company had $2.6 million of real estate owned consisting of four properties. The majority of the Company s real estate owned consisted of one real estate development project valued at $2.1 million at September 30, 2009. All these properties are being actively marketed and additional losses may occur.

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Non-Performing Assets. The table below sets forth the amounts and categories of our non-performing assets at the dates indicated.

	At September 30,				
	2009	**2008**	**2007**	**2006**	**2005**
	(Dollars in thousands)				
Non-accrual loans:					
Residential first mortgage loans:					
One- to four-family	$ 3,524	$ 1,379	$ 380	$ 436	$ 554
Construction					
Commercial	122				
Commercial real estate	580	2,531	122		
Home equity loans and lines of credit	180	28	53	40	50
Other	159				1
Total	4,565	3,938	555	476	605
Accruing loans 90 days or more past due:					
Residential first mortgage loans:					
One- to four-family					
Construction					
Commercial					
Commercial real estate					
Home equity loans and lines of credit					
Other					
Total loans 90 days or more past due					
Troubled debt restructurings	589				
Total non-performing loans	5,154	3,938	555	476	605
Real estate owned	2,579	31			19
Total non-performing assets	$ 7,733	$ 3,969	$ 555	$ 476	$ 624
Troubled debt restructurings: *					
Residential first mortgage loans:					
One- to four-family	$ 2,981	$ 149	$ 482	$ 53	$ 94
Construction					
Commercial					
Commercial real estate	180				
Home equity loans and lines of credit	7				
Other					
Total	$ 3,168	$ 149	$ 482	$ 53	$ 94
Ratios:					
Total non-performing loans to total loans	0.70%	0.55%	0.09%	0.08%	0.12%
Total non-performing loans to total assets	0.49%	0.40%	0.06%	0.07%	0.09%
Total non-performing assets to total assets	0.74%	0.40%	0.06%	0.07%	0.10%

For the year ended September 30, 2009, gross interest income that would have been recorded had our non-accruing loans been current in accordance with their original terms was $422,000.

* Non-performing troubled debt restructurings of $589,000 are included in total trouble debt restructures.

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Delinquencies. The following table sets forth certain information with respect to our loan portfolio delinquencies at the dates indicated. Loans delinquent for 90 days or more are generally classified as nonaccrual loans.

	Loans Delinquent For					
	60-89 Days		90 Days and Over		Total	
	Number	Amount	Number	Amount	Number	Amount
			(Dollars in thousands)			
At September 30, 2009						
Residential first mortgage loans:						
One- to four-family	11	$ 1,795	19	$ 3,524	30	$ 5,319
Construction						
Commercial			2	122	2	122
Commercial real estate	4	537	4	580	8	1,117
Home equity loans and lines of credit			5	180	5	180
Other	1	6	3	159	4	165
Total	16	$ 2,338	33	$ 4,565	49	$ 6,903
At September 30, 2008						
Residential first mortgage loans:						
One- to four-family	1	$ 118	9	$ 1,379	10	$ 1,497
Construction						
Commercial						
Commercial real estate			4	2,531	4	2,531
Home equity loans and lines of credit	1	37	1	28	2	65
Other						
Total	2	$ 155	14	$ 3,938	16	$ 4,093
At September 30, 2007						
Residential first mortgage loans:						
One- to four-family	2	$ 405	4	$ 380	6	$ 785
Construction						
Commercial						
Commercial real estate	1	25			1	25
Home equity loans and lines of credit			1	53	1	53
Other						
Total	3	$ 430	5	$ 433	8	$ 863
At September 30, 2006						
Residential first mortgage loans:						
One- to four-family		$	5	$ 436	5	$ 436
Construction						
Commercial						
Commercial real estate	1	49			1	49
Home equity loans and lines of credit			1	40	1	40
Other						
Total	1	$ 49	6	$ 476	7	$ 525
At September 30, 2005						
Residential first mortgage loans:						
One- to four-family	4	$ 590	8	$ 554	12	$ 1,144
Construction						
Commercial						
Commercial real estate						

Home equity loans and lines of credit	1		16	3		50	4		66
Other				1		1	1		1
Total	5	$	606	12	$	605	17	$	1,211

Classified Assets. Banking regulations and our Asset Classification Policy provide that loans and other assets considered to be of lesser quality should be classified as substandard, doubtful or loss assets. An asset is considered substandard if it is inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Substandard assets include those characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected. Assets classified as doubtful have all of the weaknesses inherent in those classified substandard, with the added characteristic that the weaknesses present make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable. Assets classified as loss are those considered uncollectible and of such little value that their continuance as assets without the establishment of a specific loss reserve is not warranted. We classify an asset as special mention if the asset has a potential weakness that warrants management s close attention. While such assets are not impaired, management has concluded that if the potential weakness in the asset is not addressed, the value of the asset may deteriorate, thereby adversely affecting the repayment of the asset.

On the basis of management s review of its assets, at September 30, 2009, we classified approximately $12.8 million of our assets as special mention, $12.9 million as substandard, $194,000 as doubtful, and none as loss.

The loan portfolio is reviewed on a regular basis to determine whether any loans require classification in accordance with applicable regulations. Not all classified assets constitute non-performing assets.

Allowance for Loan Losses

Our allowance for loan losses is maintained at a level necessary to absorb loan losses that are both probable and reasonably estimable. Management, in determining the allowance for loan losses, considers the losses inherent in its loan portfolio and changes in the nature and volume of loan activities, along with the general economic and real estate market conditions. Our allowance for loan losses consists of two elements: (1) an allocated allowance, which comprises allowances established on specific loans and class allowances based on historical loss experience and current trends, and (2) an unallocated allowance based on general economic conditions and other risk factors in our markets and portfolios. We maintain a loan review system, which allows for a periodic review of our loan portfolio and the early identification of potential impaired loans. Such system takes into consideration, among other things, delinquency status, size of loans, type and market value of collateral and financial condition of the borrowers. Specific loan loss allowances are established for identified losses based on a review of such information. A loan evaluated for impairment is considered to be impaired when, based on current information and events, it is probable that we will be unable to collect all amounts due according to the contractual terms of the loan agreement. All loans identified as impaired are evaluated independently. We do not aggregate such loans for evaluation purposes. Loan impairment is measured based on the fair value of collateral method, taking into account the appraised value, any valuation assumptions used, estimated costs to sell and trends in the market since the appraisal date. General loan loss allowances are based upon a combination of factors including, but not limited to, actual loan loss experience, composition of the loan portfolio, current economic conditions, management s judgment and losses which are probable and reasonably estimable. The allowance is increased through provisions charged against current earnings and recoveries of previously charged-off loans. Loans that are determined to be uncollectible are charged against the allowance. While management uses available information to recognize probable and reasonably estimable loan losses, future loss provisions may be necessary based on changing economic conditions. Payments received on impaired loans generally are either applied against principal or reported as interest income, according to management s judgement as to the collectability of principal. The allowance for loan losses as of September 30, 2009 is maintained at a level that represents management s best estimate of losses inherent in the loan portfolio, and such losses were both probable and reasonably estimable.

In addition, the Office of Thrift Supervision and the Pennsylvania Department of Banking, as an integral part of its examination process, periodically review our allowance for loan losses. The banking regulators may require that we recognize additions to the allowance based on its analysis and review of information available to it at the time of its examination.

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The following table sets forth activity in our allowance for loan losses for the periods indicated.

	At or For the Years Ended September 30,				
	2009	2008	2007	2006	2005
	(Dollars in thousands)				
Balance at beginning of year	$ 4,915	$ 4,206	$ 3,855	$ 3,563	$ 3,027
Charge-offs:					
Residential first mortgage loans:					
One- to four-family	(117)	(60)	(7)		(10)
Construction					
Commercial	(9)	(87)			
Commercial real estate	(457)				
Home equity loans and lines of credit	(20)	(19)	(2)	(7)	
Other		(27)	(1)	(2)	(5)
Total charge-offs	$ (603)	$ (193)	$ (10)	$ (9)	$ (15)
Recoveries:					
Residential first mortgage loans:					
One- to four-family	$	$	$	$	$
Construction					
Commercial					
Commercial real estate					
Home equity loans and lines of credit					
Other	3	2	1	1	1
Total recoveries	$ 3	$ 2	$ 1	$ 1	$ 1
Net charge-offs	$ (600)	$ (191)	$ (9)	$ (8)	$ (14)
Provision for loan losses	1,500	900	360	300	550
Balance at end of year	$ 5,815	$ 4,915	$ 4,206	$ 3,855	$ 3,563
Ratios:					
Net charge-offs to average loans outstanding	0.08%	0.03%	%	%	%
Allowance for loan losses to non-performing loans at end of year	112.82%	124.81%	757.84%	809.87%	588.93%
Allowance for loan losses to total loans at end of year	0.79%	0.69%	0.67%	0.69%	0.70%

As indicated in the table above, we charged off a de minimus amount of loans since fiscal year 2005, due, in part, to conservative underwriting of loans and aggressive monitoring of the loan portfolio to identify and address non-performing loans and potential problem assets at an early date. The amount of foreclosures we incurred in the last five years was not material to our financial statements taken as a whole and ESSA Bank & Trust suffered no material losses on foreclosed assets during that period. See Non-Performing Loans and Problem Assets. There can be no assurance that we will not experience a deterioration of our loan portfolio, including increases in non-performing loans, problem assets and charge-offs, in the future.

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Allocation of Allowance for Loan Losses. The following tables set forth the allowance for loan losses allocated by loan category, the percent of the allowance to the total allowance and the percent of loans in each category to total loans at the dates indicated. The allowance for loan losses allocated to each category is not necessarily indicative of future losses in any particular category and does not restrict the use of the allowance to absorb losses in other categories.

	2009			2008			2007		
	Amount	Percent of Allowance to Total Allowance	Percent of Loans in Category to Total Loans	Amount	Percent of Allowance to Total Allowance	Percent of Loans in Category to Total Loans	Amount	Percent of Allowance to Total Allowance	Percent of Loans in Category to Total Loans
Residential first mortgage loans:									
One- to four-family	$ 3,796	65.28%	81.70%	$ 2,862	58.23%	80.30%	$ 2,241	53.28%	79.96%
Construction	11	0.19	0.20	41	0.83	1.16	36	0.86	1.25
Commercial	248	4.27	2.20	182	3.70	1.68	177	4.21	1.23
Commercial real estate	1,116	19.19	9.20	1,222	24.86	9.76	986	23.44	9.34
Home equity loans and lines of credit	510	8.77	6.30	475	9.67	6.67	610	14.50	7.60
Other	33	0.56	0.40	30	0.61	0.43	49	1.17	0.62
Total allocated allowance	5,714	98.26	100.00	4,812	97.90	100.00	4,099	97.46	100.00
Unallocated allowance	101	1.74		103	2.10		107	2.54	
Total allowance for loan losses	$ 5,815	100.00%	100.00%	$ 4,915	100.00%	100.00%	$ 4,206	100.00%	100.00%

	2006			2005		
	Amount	Percent of Allowance to Total Allowance	Percent of Loans in Category to Total Loans	Amount	Percent of Allowance to Total Allowance	Percent of Loans in Category to Total Loans
			(Dollars in thousands)			
Residential first mortgage loans:						
One- to four-family	$ 2,026	52.56%	80.36%	$ 1,887	52.96%	81.68%
Construction	86	2.23	1.06	104	2.92	1.47
Commercial	133	3.45	1.09	114	3.20	1.03
Commercial real estate	773	20.05	8.43	471	13.22	7.17
Home equity loans and lines of credit	746	19.35	8.31	661	18.55	7.82
Other	46	1.19	0.75	39	1.09	0.83
Total allocated allowance	3,810	98.83	100.00	3,276	91.94	100.00
Unallocated allowance	45	1.17		287	8.06	
Total allowance for loan losses	$ 3,855	100.00%	100.00%	$ 3,563	100.00%	100.00%

We use the accrual method of accounting for all performing loans. The accrual of interest income is generally discontinued when the contractual payment of principal or interest has become 90 days past due or management has serious doubts about further collectibility of principal or interest, even though the loan is currently performing. When a loan is placed on nonaccrual status, unpaid interest previously credited to income is reversed. Interest received on nonaccrual loans generally is either applied against principal or reported as interest income, according to management s judgment as to the collectibility of principal. Generally, residential and consumer loans are restored to accrual status when the obligation is brought current in accordance with the contractual terms for a reasonable period of time and ultimate collectibility of total contractual principal and interest is no longer in doubt. Commercial loans are restored to accrual status when the obligation is brought current, has performed in accordance with the contractual terms for a reasonable period of time and ultimate collectibility of total contractual principal and interest no longer is in doubt.

In our collection efforts, we will first attempt to cure any delinquent loan. If a real estate secured loan is placed on nonaccrual status, it will be subject to transfer to the real estate owned (REO) portfolio (properties acquired by or in lieu of foreclosure), upon which our loan servicing department will pursue the sale of the real estate. Prior to this transfer, the loan balance will be reduced, if necessary, to reflect its current market value less estimated costs to sell. Write downs of REO that occur after the initial transfer from the loan portfolio and costs of holding the property are recorded as other operating expenses, except for significant improvements which are capitalized to the extent that the carrying value does not exceed estimated net realizable value.

Fair values for determining the value of collateral are estimated from various sources, such as real estate appraisals, financial statements and from any other reliable sources of available information. For those loans deemed to be impaired, collateral value is reduced for the estimated costs to sell. Reductions of collateral value are based on historical loss experience, current market data, and any other source of reliable information specific to the collateral.

This analysis process is inherently subjective, as it requires us to make estimates that are susceptible to revisions as more information becomes available. Although we believe that we have established the allowance at levels to absorb probable and estimable losses, future additions may be necessary if economic or other conditions in the future differ from the current environment.

Securities Activities

Our securities investment policy is established by our Board of Directors. This policy dictates that investment decisions be made based on the safety of the investment, liquidity requirements, potential returns, cash flow targets, and consistency with our interest rate risk management strategy. Our investment policy is reviewed annually by our ALCO/Investment management committee. All policy changes recommended by this management committee must be approved by the Board of Directors. The Committee is comprised of the Chief Executive Officer, Chief Financial Officer, Controller, Lending Services Division Manager, Retail Services Division Manager and the Marketing Services Manager. Authority to make investments under the approved guidelines is delegated by the Committee to appropriate officers. While general investment strategies are developed and authorized by the ALCO/Investment management committee, the execution of specific actions rests with the Chief Financial Officer.

The approved investment officers are authorized to execute investment transactions up to $5.0 million per transaction without the prior approval of the ALCO/Investment management committee and within the scope of the established investment policy. These officers are also authorized to execute investment transactions between $5.0 million and $10.0 million with the additional approval from the Chief Executive Officer. Each transaction in excess of $10.0 million must receive prior approval of the ALCO/Investment Committee.

Our current investment policy generally permits investments in debt securities issued by the U.S. government and U.S. agencies, municipal bonds, and corporate debt obligations, as well as investments in the FHLBank Pittsburgh (federal agency securities) and, to a much lesser extent, other equity securities. Securities in these categories are classified as investment securities for financial reporting purposes. The policy also permits investments in mortgage-backed securities, including pass-through securities issued and guaranteed by Fannie Mae, Freddie Mac and GNMA as well as commercial paper, corporate debt and municipal securities. Our current

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investment strategy uses a risk management approach of diversified investing in fixed-rate securities with short- to intermediate-term maturities, as well as adjustable-rate securities, which may have a longer term to maturity. The emphasis of this approach is to increase overall investment securities yields while managing interest rate risk.

Generally accepted accounting principles require that, at the time of purchase, we designate a security as held to maturity, available-for-sale, or trading, depending on our ability and intent. Securities available-for-sale are reported at fair value, while securities held to maturity are reported at amortized cost.

Mortgage-Backed Securities. We purchase mortgage-backed securities in order to generate positive interest rate spreads with minimal administrative expense, lower credit risk as a result of the guarantees provided by Freddie Mac, Fannie Mae and Government National Mortgage Association (GNMA), and increased liquidity. We invest primarily in mortgage-backed securities issued or sponsored by Fannie Mae, Freddie Mac, and GNMA. At September 30, 2009, our mortgage-backed securities portfolio had a fair value of $195.2 million, consisting of Freddie Mac, Fannie Mae and GNMA mortgage-backed securities.

Mortgage-backed securities are created by pooling mortgages and issuing a security collateralized by the pool of mortgages with an interest rate that is less than the interest rate on the underlying mortgages. Mortgage-backed securities typically represent a participation interest in a pool of single-family or multi-family mortgages, although most of our mortgage-backed securities are collateralized by single-family mortgages. The issuers of such securities (generally U.S. government agencies and U.S. government sponsored enterprises, including Fannie Mae, Freddie Mac and GNMA) pool and resell the participation interests in the form of securities to investors, such as ESSA Bank & Trust, and guarantee the payment of principal and interest to these investors. Investments in mortgage-backed securities involve a risk that actual prepayments will be greater or less than the prepayment rate estimated at the time of purchase, which may require adjustments to the amortization of any premium or accretion of any discount relating to such instruments, thereby affecting the net yield on such securities. We review prepayment estimates for our mortgage-backed securities at the time of purchase to ensure that prepayment assumptions are reasonable considering the underlying collateral for the securities at issue and current interest rates, and to determine the yield and estimated maturity of the mortgage-backed securities portfolio. Periodic reviews of current prepayment speeds are performed in order to ascertain whether prepayment estimates require modification that would cause amortization or accretion adjustments.

Equity Securities. At September 30, 2009, our equity securities were minimal.

In addition, we hold FHLBank Pittsburgh common stock to qualify for membership in the Federal Home Loan Bank System and to be eligible to borrow funds under the FHLBank Pittsburgh advance program. There is no market for the common stock.

The aggregate fair value of our FHLBank Pittsburgh common stock as of September 30, 2009 was $20.7 million based on its par value. No unrealized gains or losses have been recorded because we have determined that the par value of the common stock represents its fair value. We owned shares of FHLBank Pittsburgh common stock at September 30, 2009 with a par value that was $2.7 million more than we were required to own to maintain our membership in the Federal Home Loan Bank System and to be eligible to obtain advances. We are required to purchase additional stock as our outstanding advances increase. Any excess stock we own was redeemed monthly by the FHLBank Pittsburgh. On December 23, 2008, the FHLBank Pittsburgh notified its members, including the Company, that it was suspending the payment of dividends on its capital stock and the repurchase of excess capital stock until further notice.

We review equity and debt securities with significant declines in fair value on a periodic basis to determine whether they should be considered temporarily or other than temporarily impaired. If a decline in the fair value of a security is determined to be other than temporary, we are required to reduce the carrying value of the security to its fair value and record a non-cash, credit related impairment charge in the amount of the decline, net of tax effect, against our current income.

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Our investment securities portfolio contains unrealized losses on securities, including mortgage-related instruments issued or backed by the full faith and credit of the United States government, or generally viewed as having the implied guarantee of the United States government, and debt obligations of a State or political subdivision.

Our policy is to recognize an other-than-temporary impairment of equity securities where the fair value has been significantly below cost for four consecutive quarters. For fixed maturity investments with unrealized losses due to interest rates where the Company does not intend to sell the security and it is more likely than not that the Company will not be required to sell the security before its anticipated recovery in market value, declines in value below cost are not assumed to be other than temporary. We review our position quarterly and concluded that at September 30, 2009, declines included in the table below represent temporary declines due to interest rate change, and we do not intend to sell those securities and it more likely than not that we will not have to sell those securities before their anticipated recovery in market value. However, during the year ended September 30, 2009, the Company recognized a loss of $68,000 on equity securities that it deemed, through analysis of the security, to be other than a temporary loss. This loss was related to Fannie Mae perpetual preferred stock that the Company owns. Fannie Mae was placed into conservatorship by the U.S. Government on September 7, 2008.

The following table sets forth the composition of our securities portfolio (excluding FHLBank Pittsburgh common stock) at the dates indicated.

	At September 30,					
	2009		2008		2007	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value	Amortized Cost	Fair Value
			(Dollars in thousands)			
Investment securities available for sale:						
U.S. Government agency obligations	$ 21,458	$ 21,746	$ 48,887	$ 48,891	$ 82,297	$ 82,392
Obligations of state and political subdivisions	7,168	7,483	7,171	7,146	7,172	7,332
Mortgage-backed securities	182,448	188,264	148,199	147,945	114,840	114,613
Total debt securities	211,074	217,493	204,257	203,982	204,309	204,337
Equity securities	12	73	79	96	882	930
Total investment securities available-for-sale	$ 211,086	$ 217,566	$ 204,336	$ 204,078	$ 205,191	$ 205,267
Investment securities held-to-maturity:						
U.S. Government agency obligations	$	$	$ 2,000	$ 2,023	$ 4,731	$ 4,734
Mortgage-backed securities	6,709	6,923	9,857	9,901	12,399	12,142
Total securities held to maturity	$ 6,709	$ 6,923	$ 11,857	$ 11,924	$ 17,130	$ 16,876

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Portfolio Maturities and Yields. The composition and maturities of the investment securities portfolio at September 30, 2009 are summarized in the following table. Maturities are based on the final contractual payment dates, and do not reflect the impact of prepayments or early redemptions that may occur.

	One Year or Less		More than One Year through Five Years		More than Five Years through Ten Years		More than Ten Years		Total Securities		
	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield	Amortized Cost	Fair Value	Weighted Average Yield
	(Dollars in thousands)										
Investment securities available for sale:											
U.S. Government agency obligations	$ 503	4.62%	$ 20,955	3.38%	$	0.00%	$	0.00%	$ 21,458	$ 21,746	3.41%
Obligations of state and political subdivisions		0.00%		0.00%	996	4.00%	6,172	4.73%	7,168	7,483	4.63%
Mortgage-backed securities	824	4.33%	224	5.12%	26,124	4.21%	155,276	5.00%	182,448	188,264	4.88%
Total debt securities	$ 1,327	4.44%	$ 21,179	3.40%	$ 27,120	4.20%	$ 161,448	4.99%	$ 211,074	$ 217,493	4.73%
Equity securities	12	0.00%		0.00%		0.00%		0.00%	12	73	0.00%
Total investment securities available for-sale	$ 1,339	4.40%	$ 21,179	3.40%	$ 27,120	4.20%	$ 161,448	4.99%	$ 211,086	$ 217,566	4.72%
Investment securities held-to-maturity:											
Mortgage-backed securities	$ 1,580	4.53%	$ 1,085	4.50%	$ 2,346	4.72%	$ 1,698	3.89%	$ 6,709	$ 6,923	4.43%
Total securities held to maturity	$ 1,580	4.53%	$ 1,085	4.50%	$ 2,346	4.72%	$ 1,698	3.89%	$ 6,709	$ 6,923	4.43%

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Sources of Funds

General. Deposits, borrowings, repayments and prepayments of loans and securities, proceeds from maturing securities and cash flows from operations are the primary sources of our funds for use in lending, investing and for other general purposes.

Deposits. We offer a variety of deposit accounts with a range of interest rates and terms. Our deposit accounts consist of savings accounts, NOW accounts, checking accounts, money market accounts, club accounts, certificates of deposit and IRAs and other qualified plan accounts. We provide commercial checking accounts for businesses.

At September 30, 2009, our deposits totaled $408.9 million. Interest-bearing NOW, savings and club and money market deposits totaled $230.2 million at September 30, 2009. At September 30, 2009, we had a total of $153.2 million in certificates of deposit. Noninterest-bearing demand deposits totaled $25.4 million. Although we have a significant portion of our deposits in shorter-term certificates of deposit, we monitor activity on these accounts and, based on historical experience and our current pricing strategy, we believe we will retain a large portion of these accounts upon maturity.

Our deposits are obtained predominantly from the areas in which our branch offices are located. We rely on our favorable locations, customer service and competitive pricing to attract and retain these deposits. While we accept certificates of deposit in excess of $100,000 for which we may provide preferential rates, we generally do not solicit such deposits as they are more difficult to retain than core deposits. At September 30, 2009, we had a total of $21.9 million of brokered certificates of deposits, an increase of $11.0 million from the prior fiscal year end. Our brokered certificates of deposits range from one- to five-year terms, and are purchased only through pre-approved brokers.

The following table sets forth the distribution of average deposit accounts, by account type, at the dates indicated.

	For the Years Ended September 30,								
	2009			2008			2007		
	Average Balance	Percent	Average Rate Paid	Average Balance	Percent	Average Rate Paid	Average Balance	Percent	Average Rate Paid
Deposit type:									
Noninterest bearing demand accounts	$ 24,711	6.31%	%	$ 24,211	6.57%	%	$ 34,934	8.49%	%
Interest bearing NOW	54,262	13.86	0.08	55,073	14.91	0.07	60,826	14.79	0.07
Money market	94,835	24.21	1.68	58,034	15.72	2.90	35,351	8.60	3.12
Savings and club	63,500	16.21	0.43	62,982	17.07	0.44	75,354	18.32	0.42
Certificates of deposit	154,365	39.41	3.26	168,763	45.73	4.19	204,802	49.80	4.48
Total deposits	$ 391,673	100.00%	1.77%	$ 369,063	100.00%	2.46%	$ 411,267	100.0%	2.28%

As of September 30, 2009, the aggregate amount of outstanding certificates of deposit in amounts greater than or equal to $100,000 was approximately $66.4 million. The following table sets forth the maturity of those certificates as of September 30, 2009.

	At September 30, 2009 (In thousands)
Three months or less	$ 16,913
Over three months through six months	7,422
Over six months through one year	4,869
Over one year	37,214
Total	$ 66,418

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At September 30, 2009, $82.2 million of our certificates of deposit had maturities of one year or less. We monitor activity on these accounts and, based on historical experience and our current pricing strategy, we believe we will retain a significant portion of these accounts upon maturity.

Borrowings. Our short-term borrowings consist of Federal Home Loan Bank and Federal Reserve Bank advances. The following table sets forth information concerning balances and interest rates on all of our short-term borrowings at the dates and for the years indicated.

	At or For the Years Ended September 30,		
	2009	2008	2007
	(Dollars in thousands)		
Balance at end of year	$ 48,091	$ 39,510	$ 34,230
Maximum outstanding at any month end	$ 73,162	$ 56,183	$ 46,409
Average balance during year	$ 48,171	$ 36,150	$ 33,975
Weighted average interest rate at end of year	0.43%	2.41%	5.17%
Average interest rate during year	0.82%	3.94%	5.21%

At September 30, 2009, we had the ability to borrow approximately $481.0 million under our credit facilities with the FHLBank Pittsburgh.

Competition

We face significant competition in both originating loans and attracting deposits. The counties in which we operate have a significant concentration of financial institutions, many of which are significantly larger institutions and have greater financial resources than we, and many of which are our competitors to varying degrees. Our competition for loans comes principally from commercial banks, savings banks, mortgage banking companies, credit unions, leasing companies, insurance companies and other financial service companies. Our most direct competition for deposits has historically come from commercial banks, savings banks and credit unions. We face additional competition for deposits from nondepository competitors such as the mutual fund industry, securities and brokerage firms and insurance companies.

We seek to meet this competition by the convenience of our branch locations, emphasizing personalized banking and the advantage of local decision-making in our banking business. Specifically, we promote and maintain relationships and build customer loyalty within local communities by focusing our marketing and community involvement on the specific needs of individual neighborhoods. As of June 30, 2009, ESSA Bank & Trust had the second largest deposit market share in Monroe County, Pennsylvania. We do not rely on any individual, group, or entity for a material portion of our deposits.

Employees

As of September 30, 2009, we had 163 full-time employees and 30 part-time employees. The employees are not represented by a collective bargaining unit and we consider our relationship with our employees to be good.

Subsidiary Activities

ESSA Bank & Trust has two wholly owned subsidiaries, ESSACOR, Inc. and Pocono Investment Company. ESSACOR, Inc. is a Pennsylvania corporation that is currently inactive. Pocono Investment Company is a Delaware corporation formed as an investment company subsidiary to hold and manage certain investments of ESSA Bank & Trust, including certain intellectual property.

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SUPERVISION AND REGULATION

General

ESSA Bancorp, Inc. is a Pennsylvania corporation. As a savings and loan holding company, we are required to file certain reports with, and otherwise comply with the rules and regulations of the Office of Thrift Supervision.

ESSA Bank & Trust is a Pennsylvania-chartered savings association and its deposit accounts are insured up to applicable limits by the Federal Deposit Insurance Corporation under the Deposit Insurance Fund (DIF). We are subject to extensive regulation by the Pennsylvania Department of Banking, our chartering agency, and by the Office of Thrift Supervision, our primary federal regulator. We must file reports with the Pennsylvania Department of Banking and the Office of Thrift Supervision concerning our activities and financial condition in addition to obtaining regulatory approvals prior to entering into certain transactions including, but not limited to, mergers with or acquisitions of other savings institutions. There are periodic examinations by the Pennsylvania Department of Banking and the Office of Thrift Supervision to test our compliance with various regulatory requirements. This regulation and supervision establishes a comprehensive framework of activities in which an institution can engage and is intended primarily for the protection of the Federal Deposit Insurance Corporation insurance fund and depositors. The regulatory structure also gives the regulatory authorities extensive discretion in connection with their supervisory and enforcement activities and with their examination policies, including policies with respect to the classification of assets and the establishment of adequate loan loss reserves for regulatory purposes. Any change in such regulation, whether by the Pennsylvania Department of Banking or the Office of Thrift Supervision could have a material adverse impact on us and our operations.

Regulation by the Pennsylvania Department of Banking

The Pennsylvania Savings Association Code of 1967, as amended (the Savings Association Code) contains detailed provisions governing the organization, location of offices, rights and responsibilities of directors, officers, employees, and depositors, as well as corporate powers, savings and investment operations and other aspects of ESSA Bank & Trust and its affairs. The Savings Association Code delegates extensive rulemaking power and administrative discretion to the Pennsylvania Department of Banking so that the supervision and regulation of state-chartered savings associations may be flexible and readily responsive to changes in economic conditions and in savings and lending practices.

One of the purposes of the Savings Association Code is to provide savings associations with the opportunity to be competitive with each other and with other financial institutions existing under other Pennsylvania laws as well as other state, federal and foreign laws. A Pennsylvania savings association may locate or change the location of its principal place of business and establish an office anywhere in Pennsylvania, with the prior approval of the Pennsylvania Department of Banking.

The Pennsylvania Department of Banking generally examines each savings association not less frequently than once every two years. Although the Department may accept the examinations and reports of the Office of Thrift Supervision in lieu of the Department s examination, the current practice is for the Department to conduct individual examinations. The Department may order any savings association to discontinue any violation of law or unsafe or unsound business practice and may direct any trustee, officer, attorney, or employee of a savings association engaged in an objectionable activity, after the Department has ordered the activity to be terminated, to show cause at a hearing before the Department why such person should not be removed.

Regulation by the Office of Thrift Supervision

ESSA Bank & Trust is also subject to extensive regulation, examination and supervision by the Office of Thrift Supervision, as its primary federal regulator. Such regulation and supervision:

- establishes a comprehensive framework of activities in which ESSA Bank & Trust can engage;
- limits the ability of ESSA Bank & Trust to extend credit to any given borrower;

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significantly limits the transactions in which ESSA Bank & Trust may engage with its affiliates;

requires ESSA Bank & Trust to meet a qualified thrift lender test which requires ESSA Bank & Trust to invest in qualified thrift investments, which include primarily residential mortgage loans and related investments;

places limitations on capital distributions by savings associations, such as ESSA Bank & Trust, including cash dividends;

imposes assessments to the Office of Thrift Supervision to fund its operations;

establishes a continuing and affirmative obligation, consistent with ESSA Bank & Trust s safe and sound operation, to help meet the credit needs of its community, including low and moderate income neighborhoods;

establishes various capital categories resulting in various levels of regulatory scrutiny applied to the institutions in a particular category; and

establishes standards for safety and soundness.

The Office of Thrift Supervision generally examines each savings association not less frequently than once every two years. The Office of Thrift Supervision has the authority to order any savings association or its directors, trustees, officers, attorneys or employees to discontinue any violation of law or unsafe or unsound banking practice.

Transactions with Affiliates

Sections 23A and 23B of the Federal Reserve Act and its implementing regulations govern transactions between depository institutions and their affiliates. These provisions are made applicable to savings associations, such as ESSA Bank & Trust, by the Home Owners Loan Act and Office of Thrift Supervision regulation. In a holding company context, the parent holding company of a savings association and any companies that are controlled by the parent holding company are affiliates of the savings association.

Section 23A limits the extent to which a savings association or its subsidiaries may engage in certain transactions with its affiliates. These transactions include, among other things, the making of loans or other extensions of credit to an affiliate and the purchase of assets from an affiliate. Generally, these transactions between the savings association and any one affiliate cannot exceed 10% of the savings association s capital stock and surplus, and these transactions between the savings institution and all of its affiliates cannot, in the aggregate, exceed 20% of the savings institution s capital stock and surplus. Section 23A also establishes specific collateral requirements for loans or extensions of credit to an affiliate, and for guarantees or acceptances on letters of credit issued on behalf of an affiliate. Applicable regulations prohibit a savings association from lending to any affiliate engaged in activities not permissible for a bank holding company or for the purpose of acquiring the securities of most affiliates.

Section 23B requires that transactions covered by Section 23A and a broad list of other specified transactions be on terms and under circumstances substantially the same, or no less favorable to the savings association or its subsidiary, as similar transactions with non-affiliates. In addition to the restrictions on transactions with affiliates that Sections 23A and 23B of the Federal Reserve Act impose on depository institutions, the regulations of the Office of Thrift Supervision also generally prohibit a savings association from purchasing or investing in securities issued by an affiliate.

Insurance of Accounts and Regulation by the Federal Deposit Insurance Corporation

Deposit accounts in ESSA Bank & Trust are insured by the Federal Deposit Insurance Corporation (FDIC) generally up to a maximum of $100,000 per separately insured depositor and up to a maximum of $250,000 for self-directed retirement accounts. ESSA Bank & Trust s deposits, therefore, are subject to FDIC deposit insurance assessments.

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The Emergency Economic Stabilization Act which became law on October 3, 2008 raised the amount of federal deposit insurance coverage for all deposit accounts to $250,000. This provision of the Act is scheduled to expire on December 31, 2013. In addition, on October 14, 2008 the FDIC announced a new program the Temporary Liquidity Guarantee Program, which provides FDIC coverage on non-interest bearing deposit transaction accounts and certain other accounts regardless of dollar amount. This new program is scheduled to expire June 30, 2010.

The Federal Deposit Insurance Corporation regulations assess insurance premiums based on an institution s risk. Under this assessment system, the Federal Deposit Insurance Corporation evaluates the risk of each financial institution based on its supervisory rating, financial ratios, and long-term debt issuer rating. The rates for nearly all of the financial institutions industry vary between five and seven cents for every $100 of domestic deposits. Federal law requires the Federal Deposit Insurance Corporation to establish a deposit reserve ratio for the deposit insurance fund of between 1.15% and 1.50% of estimated deposits.

Effective March 31, 2006, the Federal Deposit Insurance Corporation merged the Bank Insurance Fund (BIF) and the Savings Association Insurance Fund (SAIF) into a single fund called the Deposit Insurance Fund. In addition to the Federal Deposit Insurance Corporation assessments, the Financing Corporation (FICO) is authorized to impose and collect, with the approval of the Federal Deposit Insurance Corporation, assessments for anticipated payments, issuance costs and custodial fees on bonds issued by the FICO in the 1980s to recapitalize the Federal Savings and Loan Insurance Corporation. The bonds issued by the FICO are due to mature in 2017 through 2019. For the quarter ended June 30, 2009, the annualized FICO assessment was equal to 1.14 basis points for each $100 in domestic deposits maintained at an institution.

Recent failures have significantly increased the Deposit Insurance Fund s (the DIF or the fund) loss provisions, resulting in a decline in the reserve ratio. As of June 30, 2009, the reserve ratio stood at 0.22%, Staff expects a higher rate of insured institution failures in the next few years compared to recent years; thus, the reserve ratio may continue to decline. Because the fund reserve ratio has fallen below 1.15% and is expected to remain below 1.15%, the FDIC is required to establish and implement a restoration plan to restore the reserve ratio to 1.15%. Absent extraordinary circumstances, the reserve ratio must be returned to at least 1.15% no later than five years after establishment of the plan.

On May 22, 2009, the FDIC adopted a final rule levying a five basis point special assessment on each insured depository institution s assets minus Tier 1 capital as of June 30, 2009. The special assessment was payable on September 30, 2009. We recorded an expense of $400,000 during the quarter ended June 30, 2009 to reflect the special assessment. On September 20, 2009, the FDIC increased assessment rates on deposit insurance premiums by three basis points effective January 1, 2011.

In addition, on November 12, 2009, the FDIC issued a final rule requiring all insured depository institutions to prepay their estimated assessments for the fourth quarter of 2009, and for all of 2010, 2011 and 2012, on December 30, 2009. Under the terms of the new rule, we will be required to make a payment of approximately $1.9 million to the FDIC on December 30, 2009. We will record the payment as a prepaid expense, which will be amortized to expense over three years.

Capital Requirements

Any savings institution that fails any of the capital requirements is subject to possible enforcement actions by the Office of Thrift Supervision. Such actions could include a capital directive, a cease and desist order, civil money penalties, the establishment of restrictions on an institution s operations, termination of federal deposit insurance, and the appointment of a conservator or receiver. Certain actions are required by law. The Office of Thrift Supervision s capital regulation provides that such actions, through enforcement proceedings or otherwise, could require one or more of a variety of corrective actions.

We are also subject to more stringent capital guidelines of the Pennsylvania Department of Banking. Although not adopted in regulation form, the Pennsylvania Department of Banking utilizes capital standards of 6% leverage capital and 10% risk-based capital. The components of leverage and risk-based capital are substantially the same as those defined by the Office of Thrift Supervision.

Loans-to-One-Borrower Limitation

Under federal regulations, with certain limited exceptions, a Pennsylvania chartered savings association may lend to a single or related group of borrowers on an unsecured basis an amount equal to 15% of its unimpaired capital and surplus. An additional amount, equal to 10% of unimpaired capital and surplus, may be lent if such loan is secured by readily marketable collateral, which is defined to include certain securities, but generally does not include real estate. Our internal policy, however, is to not make a commercial loan in excess of $5.0 million, nor to allow more than $7.5 million in total loan relationships with any one borrower, including the borrower s residential mortgage and consumer loans. However, in special circumstances this limit may be exceeded subject to the approval of the Management Loan Committee in addition to a majority of the members of the Board of Directors.

Prompt Corrective Action

Under federal regulations, a savings association is deemed to be (i) well capitalized if it has total risk-based capital of 10.0% or more, has a Tier 1 risk-based capital ratio of 6.0% or more, has a Tier I leverage capital ratio of 5.0% or more and is not subject to any written capital order or directive; (ii) adequately capitalized if it has a total risk-based capital ratio of 8.0% or more, a Tier I risk-based capital ratio of 4.0% or more and a Tier I leverage capital ratio of 4.0% or more (3.0% under certain circumstances) and does not meet the definition of well capitalized ; (iii) undercapitalized if it has a total risk-based capital ratio that is less than 8.0%, a Tier I risk-based capital ratio that is less than 4.0% or a Tier I leverage capital ratio that is less than 4.0% (3.0% under certain circumstances); (iv) significantly undercapitalized if it has a total risk-based capital ratio that is less than 6.0%, a Tier I risk-based capital ratio that is less than 3.0% or a Tier I leverage capital ratio that is less than 3.0%; and (v) critically undercapitalized if it has a ratio of tangible equity to total assets that is equal to or less than 2.0%. Federal regulations also specify circumstances under which a federal banking agency may reclassify a well capitalized institution as adequately capitalized and may require an adequately capitalized institution to comply with supervisory actions as if it were in the next lower category (except that the Office of Thrift Supervision may not reclassify a significantly undercapitalized institution as critically undercapitalized). As of September 30, 2009, the Bank was a well-capitalized institution for this purpose.

The USA PATRIOT Act

The USA PATRIOT Act of 2001 gave the federal government new powers to address terrorist threats through enhanced domestic security measures, expanded surveillance powers, increased information sharing and broadened anti-money laundering requirements. The USA PATRIOT Act also required the federal banking agencies to take into consideration the effectiveness of controls designed to combat money laundering activities in determining whether to approve a merger or other acquisition application of a member institution. Accordingly, if we engage in a merger or other acquisition, our controls designed to combat money laundering would be considered as part of the application process. We have established policies, procedures and systems designed to comply with these regulations.

Holding Company Regulation

ESSA Bancorp, Inc. is a unitary savings and loan holding company, subject to regulation and supervision by the Office of Thrift Supervision. The Office of Thrift Supervision will have enforcement authority over ESSA Bancorp, Inc. and its non-savings institution subsidiaries. Among other things, this authority permits the Office of Thrift Supervision to restrict or prohibit activities that are determined to be a risk to ESSA Bank & Trust.

Under prior law, a unitary savings and loan holding company generally had no regulatory restrictions on the types of business activities in which it could engage, provided that its subsidiary savings association was a qualified thrift lender. The Gramm-Leach-Bliley Act of 1999, however, restricts unitary savings and loan holding companies not existing on, or applied for before, May 4, 1999 to those activities permissible for financial holding companies or for multiple savings and loan holding companies. The Company is not a grandfathered unitary savings and loan holding company and, therefore, is limited to the activities permissible for financial holding companies or for multiple savings and loan holding companies. A financial holding company may engage in activities that are financial in nature, including underwriting equity securities and insurance as well as activities that are incidental to financial activities or complementary to a financial activity. A multiple savings and loan holding company is generally limited to activities permissible for bank holding companies under Section 4(c)(8) of the Bank Holding Company Act, subject to the prior approval of the Office of Thrift Supervision, and certain additional activities authorized by Office of Thrift Supervision regulations.

Federal law prohibits a savings and loan holding company, directly or indirectly, or through one or more subsidiaries, from acquiring control of another savings institution or holding company thereof, without prior written approval of the Office of Thrift Supervision. It also prohibits the acquisition or retention of, with specified exceptions, more than 5% of the equity securities of a company engaged in activities that are not closely related to banking or financial in nature or acquiring or retaining control of an institution that is not federally insured. In evaluating applications by holding companies to acquire savings institutions, the Office of Thrift Supervision must consider the financial and managerial resources and future prospects of the savings institution involved, the effect of the acquisition on the risk to the insurance fund, the convenience and needs of the community, the effectiveness of each parties anti-money laundering program, and competitive factors.

Federal Securities Laws

Shares of ESSA Bancorp, Inc. s common stock are registered with the SEC under Section 12(b) of the Securities Exchange Act of 1934, as amended (the Exchange Act). ESSA Bancorp, Inc. is also subject to the proxy rules, tender offer rules, insider trading restrictions, annual and periodic reporting, and other requirements of the Exchange Act.

Sarbanes-Oxley Act of 2002

The Sarbanes-Oxley Act of 2002 was enacted in response to public concerns regarding corporate accountability in connection with certain accounting scandals. The stated goals of the Sarbanes-Oxley Act are to increase corporate responsibility, to provide for enhanced penalties for accounting and auditing improprieties at publicly traded companies, and to protect investors by improving the accuracy and reliability of corporate disclosures pursuant to the securities laws. The Sarbanes-Oxley Act generally applies to all companies that file or are required to file periodic reports with the Securities and Exchange Commission, under the Securities Exchange Act of 1934.

The Sarbanes-Oxley Act includes specific additional disclosure requirements, requires the Securities and Exchange Commission and national securities exchanges to adopt extensive additional disclosure, corporate governance and other related rules, and mandates further studies of certain issues by the Securities and Exchange Commission. The Sarbanes-Oxley Act represents significant federal involvement in matters traditionally left to state regulatory systems, such as the regulation of the accounting profession, and to corporate law, such as the relationship between a board of directors and management and between a board of directors and its committees.

Although we have and will continue to incur additional expense in complying with the provisions of the Sarbanes-Oxley Act and the resulting regulations, management does not expect that such compliance will have a material impact on our results of operations or financial condition.

Regulatory Enforcement Authority

Federal law provides federal banking regulators with substantial enforcement powers. This enforcement authority includes, among other things, the ability to assess civil money penalties, to issue cease-and-desist or removal orders, and to initiate injunctive actions against banking organizations and institution-affiliated parties, as defined. In general, these enforcement actions may be initiated for violations of laws and regulations and unsafe or unsound practices. Other actions or inactions may provide the basis for enforcement action, including misleading or untimely reports filed with regulatory authorities.

Dividends

Our ability to pay dividends depends, to a large extent, upon ESSA Bank & Trust s ability to pay dividends to ESSA Bancorp. The Savings Association Code states, in part, that dividends may be declared and paid by the Bank only out of net earnings for the then current year. A dividend may not be declared or paid if it would impair the general reserves of ESSA Bank & Trust required to be maintained under the Savings Association Code. In

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addition, we are required to notify the Office of Thrift Supervision prior to declaring a dividend to the Company, and receive the nonobjection of the Office of Thrift Supervision to any such dividend.

FEDERAL AND STATE TAXATION

Federal Taxation

General. ESSA Bancorp, Inc. and ESSA Bank & Trust are subject to federal income taxation in the same general manner as other corporations, with some exceptions discussed below. The following discussion of federal taxation is intended only to summarize material federal income tax matters and is not a comprehensive description of the tax rules applicable to ESSA Bancorp, Inc. and ESSA Bank & Trust.

Method of Accounting. For federal income tax purposes, ESSA Bancorp, Inc. currently reports its income and expenses on the accrual method of accounting and uses a tax year ending September 30th for filing its consolidated federal income tax returns. The Small Business Protection Act of 1996 eliminated the use of the reserve method of accounting for bad debt reserves by savings institutions, effective for taxable years beginning after 1995.

Bad Debt Reserves. Prior to the Small Business Protection Act of 1996, ESSA Bank & Trust was permitted to establish a reserve for bad debts for tax purposes and to make annual additions to the reserve. These additions could, within specified formula limits, be deducted in arriving at ESSA Bank & Trust s taxable income. As a result of the Small Business Protection Act of 1996, ESSA Bank & Trust must use the specific charge off method in computing its bad debt deduction for tax purposes.

Taxable Distributions and Recapture. Prior to the Small Business Protection Act of 1996, bad debt reserves created prior to 1988 were subject to recapture into taxable income if ESSA Bank & Trust failed to meet certain thrift asset and definition tests. The Small Business Protection Act of 1996 eliminated these thrift-related recapture rules. However, under current law, pre-1988 reserves remain subject to tax recapture should ESSA Bank & Trust make certain distributions from its tax bad debt reserve or cease to maintain a financial institution charter. At September 30, 2009, ESSA Bank & Trust s total federal pre-1988 reserve was approximately $4.3 million. This reserve reflects the cumulative effects of federal tax deductions by ESSA Bank & Trust for which no federal income tax provision has been made.

Minimum Tax. The Internal Revenue Code of 1986, as amended, imposes an alternative minimum tax at a rate of 20% on a base of regular taxable income plus certain tax preferences, referred to as alternative minimum taxable income. The alternative minimum tax is payable to the extent alternative minimum tax income is in excess of the regular income tax. Net operating losses can, in general, offset no more than 90% of alternative minimum taxable income. Certain payments of alternative minimum tax may be used as credits against regular tax liabilities in future years. At September 30, 2009, ESSA Bank & Trust had no minimum tax credit carryforward.

Net Operating Loss Carryovers. A financial institution may carry back net operating losses to the preceding two taxable years (five years for losses incurred in 2001, 2002 and 2009) and forward to the succeeding 20 taxable years. At September 30, 2009, ESSA Bank & Trust had no net operating loss carryforward for federal income tax purposes.

Corporate Dividends. We may exclude from our income 100% of dividends received from ESSA Bank & Trust as a member of the same affiliated group of corporations.

Audit of Tax Returns. ESSA Bank & Trust s federal income tax returns have not been audited in the most recent five-year period. The 2006, 2007 and 2008 tax years remain open.

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State Taxation

Pennsylvania State Taxation. ESSA Bancorp, Inc. is subject to the Pennsylvania Corporate Net Income Tax, Capital Stock and Franchise Tax. The Corporation Net Income Tax rate for 2009 is 9.9% and is imposed on unconsolidated taxable income for federal purposes with certain adjustments. In general, the Capital Stock and Franchise Tax is a property tax imposed on a corporation s capital stock value at a statutorily defined rate, such value being determined in accordance with a fixed formula based upon average net income and net worth. ESSA Bank & Trust is subject to tax under the Pennsylvania Mutual Thrift Institutions Tax Act, as amended to include thrift institutions having capital stock. Pursuant to the Mutual Thrift Institutions Tax, the tax rate is 11.5%. The Mutual Thrift Institutions Tax exempts ESSA Bank & Trust from other taxes imposed by the Commonwealth of Pennsylvania for state income tax purposes and from all local taxation imposed by political subdivisions, except taxes on real estate and real estate transfers. The Mutual Thrift Institutions Tax is a tax upon net earnings, determined in accordance with generally accepted accounting principles with certain adjustments. The Mutual Thrift Institutions Tax, in computing income according to generally accepted accounting principles, allows for the deduction of interest earned on state and federal obligations, while disallowing a percentage of a thrift s interest expense deduction in the proportion of interest income on those securities to the overall interest income of ESSA Bank & Trust. Net operating losses, if any, thereafter can be carried forward three years for Mutual Thrift Institutions Tax purposes.

Item 1A. Risk Factors

Increases to the Allowance for Credit Losses May Cause Our Earnings to Decrease.

Our customers may not repay their loans according to the original terms, and the collateral securing the payment of those loans may be insufficient to pay any remaining loan balance. In addition, the estimates used to determine the fair value of such loans as of the acquisition date may be inconsistent with the actual performance of the acquired loans. Hence, we may experience significant credit losses, which could have a material adverse effect on our operating results. We make various assumptions and judgments about the collectibility of our loan portfolio, including the creditworthiness of our borrowers and the value of the real estate and other assets serving as collateral for the repayment of loans. In determining the amount of the allowance for credit losses, we rely on loan quality reviews, past loss experience, and an evaluation of economic conditions, among other factors. If our assumptions prove to be incorrect, our allowance for credit losses may not be sufficient to cover losses inherent in our loan portfolio, resulting in additions to the allowance. Material additions to the allowance would materially decrease our net income.

Our emphasis on the origination of commercial real estate and business loans is one of the more significant factors in evaluating our allowance for credit losses. As we continue to increase the amount of these loans, additional or increased provisions for credit losses may be necessary and as a result would decrease our earnings.

Bank regulators periodically review our allowance for credit losses and may require us to increase our provision for credit losses or loan charge-offs. Any increase in our allowance for credit losses or loan charge-offs as required by these regulatory authorities could have a material adverse effect on our results of operations and/or financial condition.

Future Changes in Interest Rates Could Reduce Our Profits.

Our ability to make a profit largely depends on our net interest income, which could be negatively affected by changes in interest rates. Net interest income is the difference between:

1. the interest income we earn on our interest-earning assets, such as loans and securities; and

2. the interest expense we pay on our interest-bearing liabilities, such as deposits and borrowings.

From September, 2007 through December, 2008, the Federal Reserve Board of Governors decreased its target for the federal funds rate from 5.25% to 0.25%. The federal funds rate remained at 0.25% through November, 2009 and is expected to remain at or around that level for an extended period of time. While these short term market interest rates (which we use as a guide to price our deposits) decreased, longer term market interest rates (which we

use as a guide to price our longer term loans) did not decrease to the same degree. As a result of this steepening of the market yield curve the Company s net interest spread has increased from 2.28% for the quarter ended December 31, 2008 to 2.42% for the quarter ended September 30, 2009. If this steepening were to continue the initial increase in our interest rate spread would be reduced as our assets continue to re-price downward.

In addition, changes in interest rates can affect the average life of loans and mortgage-backed and related securities. A reduction in interest rates results in increased prepayments of loans and mortgage-backed and related securities, as borrowers refinance their loans in order to reduce their borrowing costs. This creates reinvestment risk, which is the risk that we may not be able to reinvest prepayments at rates that are comparable to the rates we earned on the prepaid loans or securities. Alternatively, increases in interest rates may decrease loan demand and/or make it more difficult for borrowers to repay adjustable rate loans.

Changes in interest rates also affect the current market value of our interest-earning securities portfolio. Generally, the value of securities moves inversely with changes in interest rates. At September 30, 2009, the fair value of our debt securities available for sale totaled $217.5 million. Unrealized net gains on these available for sale securities totaled approximately $6.4 million at September 30, 2009 and are reported as a separate component of stockholders equity. Decreases in the fair value of securities available for sale in future periods would have an adverse effect on stockholders equity.

We evaluate interest rate sensitivity by estimating the change in ESSA Bank & Trust s net portfolio value over a range of interest rate scenarios. Net portfolio value is the discounted present value of expected cash flows from assets, liabilities and off-balance sheet contracts. At September 30, 2009, in the event of an immediate 200 basis point increase in interest rates, the Office of Thrift Supervision model projects that we would experience a $21.2 million, or 12.0%, decrease in net portfolio value. See Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations Management of Market Risk.

A Downturn in the Local Economy or a Decline in Real Estate Values Could Reduce Our Profits.

Nearly all of our real estate loans are secured by real estate in Monroe and Northampton Counties, Pennsylvania. As a result of this concentration, a prolonged downturn in this market area could cause significant increases in nonperforming loans, which would reduce our profits. Additionally, a decrease in asset quality could require additions to our allowance for loan losses through increased provisions for loan losses, which would hurt our profits. A decline in real estate values could cause some of our mortgage loans to become inadequately collateralized, which would expose us to a greater risk of loss. For a discussion of our market area, see Item 1. Business Market Area.

Recent Negative Developments in the Financial Industry and the Domestic and International Credit Markets may Adversely Affect our Operations and Results.

Negative developments in the latter half of 2007, during 2008 and continuing through 2009 in the global credit and securitization markets have resulted in uncertainty in the financial markets in general with the expectation of the general economic downturn continuing into 2010. Loan portfolio quality has deteriorated at many institutions. In addition, the values of real estate collateral supporting many commercial loans and home mortgages have declined and may continue to decline. Bank and bank holding company stock prices have been negatively affected, as has the ability of banks and bank holding companies to raise capital or borrow in the debt markets. As a result, the potential exists for new federal or state laws and regulations regarding lending and funding practices and liquidity standards, and bank regulatory agencies are expected to be active in responding to concerns and trends identified in examinations, including the expected issuance of many formal enforcement orders. Negative developments in the financial industry and the domestic and international credit markets, and the impact of new legislation in response to those developments, may negatively impact our operations by restricting our business operations, including our ability to originate or sell loans, and adversely impact our financial performance. In addition, these risks could affect the value of our loan portfolio as well as the value of our investment portfolio, which would also negatively affect our financial performance.

Our Continued Emphasis On Commercial Real Estate Lending Increases Our Exposure To Increased Lending Risks.

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Our business strategy centers on continuing our emphasis on commercial real estate lending. We have grown our loan portfolio in recent years with respect to this type of loan and intend to continue to emphasize this type of lending. At September 30, 2009, $68.0 million, or 9.2%, of our total loan portfolio consisted of commercial real estate loans. Loans secured by commercial real estate generally expose a lender to greater risk of non-payment and loss than one- to four-family residential mortgage loans because repayment of the commercial real estate loans often depends on the successful operation of the property and the income stream of the underlying property. Additionally, such loans typically involve larger loan balances to single borrowers or groups of related borrowers compared to one- to four-family residential mortgage loans. Accordingly, an adverse development with respect to one loan or one credit relationship can expose us to greater risk of loss compared to an adverse development with respect to a one- to four-family residential mortgage loan. We seek to minimize these risks through our underwriting policies, which require such loans to be qualified on the basis of the property s collateral value, net income and debt service ratio; however, there is no assurance that our underwriting policies will protect us from credit-related losses.

At September 30, 2009, our largest commercial real estate lending relationship was $4.1 million of loans located in Monroe County, Pennsylvania and secured by real estate. See Item 1. Business Lending Activities Commercial Real Estate Loans.

Strong Competition Within Our Market Areas May Limit Our Growth and Profitability.

Competition in the banking and financial services industry is intense. In our market areas, we compete with commercial banks, savings institutions, mortgage brokerage firms, credit unions, finance companies, mutual funds, insurance companies, and brokerage and investment banking firms operating locally and elsewhere. Some of our competitors have greater name recognition and market presence that benefit them in attracting business, and offer certain services that we do not or cannot provide. In addition, larger competitors may be able to price loans and deposits more aggressively than we do, which could affect our ability to grow and remain profitable on a long-term basis. Our profitability depends upon our continued ability to successfully compete in our market areas. For additional information see Item 1. Business Competition.

Economic Conditions May Adversely Affect Our Liquidity and Financial Condition.

Recent significant declines in the values of mortgage-backed securities and derivative securities issued by financial institutions, government sponsored entities, and major commercial and investment banks have led to decreased confidence in financial markets among borrowers, lenders, and depositors, as well as disruption and extreme volatility in the capital and credit markets and the failure of some entities in the financial sector. As a result, many lenders and institutional investors have reduced or ceased to provide funding to borrowers. Continued turbulence in the capital and credit markets may adversely affect our liquidity and financial condition and the willingness of certain counterparties and customers to do business with us.

We Operate in a Highly Regulated Environment and May Be Adversely Affected by Changes in Laws and Regulations.

We are subject to extensive regulation, supervision, and examination by the Office of Thrift Supervision (the OTS), the FDIC and the Pennsylvania Department of Banking. Such regulators govern the activities in which we may engage, primarily for the protection of depositors. These regulatory authorities have extensive discretion in connection with their supervisory and enforcement activities, including the imposition of restrictions on the operation of a bank, the classification of assets by a bank, the imposition of higher capital requirements, and the adequacy of a bank s allowance for credit losses. Any change in such regulation and oversight, whether in the form of regulatory policy, regulations, or legislation, could have a material impact on us and our operations. We believe that we are in substantial compliance with applicable federal, state and local laws, rules and regulations. Because our business is highly regulated, the laws, rules and applicable regulations are subject to regular modification and change. There can be no assurance that proposed laws, rules and regulations, or any other laws, rules or regulations, will not be adopted in the future, which could make compliance more difficult or expensive or otherwise adversely affect our business, financial condition or prospects.

The Soundness of Other Financial Services Institutions May Adversely Affect Our Credit Risk.

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We rely on other financial services institutions through trading, clearing, counterparty, and other relationships. We maintain limits and monitor concentration levels of our counterparties as specified in our internal policies. Our reliance on other financial services institutions exposes us to credit risk in the event of default by these institutions or counterparties. These losses could adversely affect our results of operations and financial condition.

Any Future FDIC Insurance Premiums or Required Prepayments of Assessments Will Adversely Impact Our Earnings.

On May 22, 2009, the FDIC adopted a final rule levying a five basis point special assessment on each insured depository institution s assets minus Tier 1 capital as of June 30, 2009. The special assessment was payable on September 30, 2009. We recorded an expense of $400,000 during the quarter ended June 30, 2009 to reflect the special assessment. In lieu of another special assessment, on September 27, 2009, the FDIC board proposed a requirement that insured institutions prepay their estimated quarterly risk-based assessments for the fourth quarter of 2009, as well as for all of 2010, 2011 and 2012, and, in addition, increased assessment rates on deposit insurance premiums by three basis points effective January 1, 2011.

FDIC guidance provides that as of December 31, 2009, and each quarter thereafter, each insured institution will be required to record an expense for its regular quarterly assessment and an offsetting credit to the prepaid assessment until the asset is exhausted. Once the asset is exhausted, the institution would resume paying and accounting for quarterly deposit insurance assessments as it currently does. Any further special assessments that the FDIC levies will be recorded as an expense during the appropriate period. The prepayment of the future premiums, coupled with any future assessments, could have a material adverse effect on our results of operations and/or financial condition.

A Substantial Decline in the Value of Our FHLBank Pittsburgh Common Stock May Adversely Affect Our Financial Condition.

We own common stock of the FHLBank Pittsburgh (FHLB) in order to qualify for membership in the Federal Home Loan Bank system, which enables us to borrow funds under the Federal Home Loan Bank advance program. The carrying value and fair market value of our FHLB common stock was $20.7 million as of September 30, 2009.

Recent published reports indicate that certain member banks of the Federal Home Loan Bank system may be subject to asset quality risks that could result in materially lower regulatory capital levels. In an extreme situation, it is possible that the capitalization of a Federal Home Loan Bank, including the FHLB, could be substantially diminished or reduced to zero. Consequently, given that there is no market for our FHLB common stock, we believe that there is a risk that our investment could be deemed other than temporarily impaired at some time in the future. If this occurs, it may adversely affect our results of operations and financial condition.

If the capitalization of the FHLB is substantially diminished and if it reduces or suspends its dividend, our liquidity may be adversely impaired if we are not able to obtain an alternative source of funding.

Item 1B. Unresolved Staff Comments

Not applicable.

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Item 2. Properties

The following table provides certain information as of September 30, 2009 with respect to our main office located in Stroudsburg, Pennsylvania, and our thirteen full service branch offices.

Location	Leased or Owned	Year Acquired or Leased	Square Footage
Main Office:			
200 Palmer Street			
Stroudsburg, PA 18360	Owned	2003	36,000
Full Service Branches:			
Route 940			
HC 1 Box 1192			
Blakeslee, PA 18610	Owned	2002	2,688
Route 209 & Lake Mineola Road			
P.O. Box 35			
Brodheadsville, PA 18301	Owned	1983	4,100
Route 209			
7001 Milford Road			
East Stroudsburg, PA 18324	Leased	1997	1,700
Routes 209 & 447			
695 North Courtland Street			
East Stroudsburg, PA 18301	Leased	1999	420
75 Washington Street			
East Stroudsburg, PA 18301	Owned	1966	3,300
Route 209			
P.O. Box 1009			
Marshalls Creek, PA 18335	Leased	1991	2,627
Mount Pocono Plaza			
601 Route 940			
Mt. Pocono, PA 18344	Leased	1999	536
1309 Blue Valley Drive	Leased	2001	444

Pen Argyl, PA 18072			
744 Main Street			
P.O. Box L			
Stroudsburg, PA 18360	Owned	1985	12,000
Route 611			
1070 North Ninth Street			
Stroudsburg, PA 18360	Leased	2000	488

Route 611 RR1 Box 402 Tannersville, PA 18372	Leased	1993	611
Route 209 & Weir Lake Road P.O. Box 271 Brodheadsville, PA 18322	Leased	1997	576
Route 611 Tannersville Plaza Tannersville, PA 18372	Leased	2007	2,500
Other Properties			
746-752 Main Street Stroudsburg, PA 18360	Owned	2005	4,650

The net book value of our premises, land and equipment was $10.6 million at September 30, 2009.

Item 3. Legal Proceedings

The Company and its subsidiaries are subject to various legal actions arising in the normal course of business. In the opinion of management, the resolution of these legal actions is not expected to have a material adverse effect on the Company s results of operations.

Item 4. Submission of Matters to a Vote of Security Holders

During the fourth quarter of the fiscal year covered by this report, the Company did not submit any matters to the vote of security holders.

PART II

Item 5. Market for Registrant s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Our shares of common stock are traded on the Nasdaq Global Market under the symbol ESSA . The approximate number of holders of record of ESSA Bancorp, Inc. s common stock as of September 30, 2009 was 2532. Certain shares of ESSA Bancorp, Inc. are held in nominee or street name and accordingly, the number of beneficial owners of such shares is not known or included in the foregoing number. The following tables present quarterly market information for ESSA Bancorp, Inc. s common stock for the periods ended September 30, 2008 and September 30, 2009. The following information was provided by the Nasdaq Stock Market.

Fiscal 2009	High	Low	Dividends
Quarter ended September 30, 2009	$ 13.90	$ 12.53	$ 694,000
Quarter ended June 30, 2009	14.07	12.82	551,000
Quarter ended March 31, 2009	14.25	11.40	558,000
Quarter ended December 31, 2008	14.13	11.13	594,000

Fiscal 2008	High	Low	Dividends
Quarter ended September 30, 2008	$ 14.10	$ 12.90	$ 625,000
Quarter ended June 30, 2008	12.95	11.50	625,000
Quarter ended March 31, 2008	12.17	10.50	
Quarter ended December 31, 2007	11.90	9.56	

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The Board of Directors has the authority to declare cash dividends on shares of common stock, subject to statutory and regulatory requirements. We began to pay quarterly cash dividends in the third quarter of fiscal 2008. In determining whether and in what amount to pay a cash dividend in the future, the Board will take into account a number of factors, including capital requirements, our consolidated financial condition and results of operations, tax considerations, statutory and regulatory limitations and general economic conditions. No assurances can be given that cash dividends will not be reduced or eliminated in the future.

The sources of funds for the payment of a cash dividend are the retained proceeds form the initial sale of shares of common stock and earnings on those proceeds, interest and principal payments with respect to ESSA Bancorp, Inc. s loan to the Employee Stock Ownership Plan, and dividends from ESSA Bank & Trust. For a discussion of the limitations applicable to ESSA Bank & Trust s ability to pay dividends, see Business Supervision and Regulation.

Stock Performance Graph

Set forth hereunder is a stock performance graph comparing (a) the cumulative total return on the common stock between April 4, 2007 and September 30, 2009, (b) the cumulative total return on stock included in the SNL Thrift Index over such period, and (c) the cumulative total return on stocks included in the Russell 2000 Index over such period. Cumulative return assumes the reinvestment of dividends, and is expressed in dollars based on an assumed investment of $100.

There can be no assurance that the ESSA Bancorp, Inc. s stock performance will continue in the future with the same or similar trend depicted in the graph. ESSA Bancorp, Inc. will not make or endorse any predictions as to future stock performance.

ESSA BANCORP, INC.

	Period Ending										
Index	**04/04/07**	**06/30/07**	**09/30/07**	**12/31/07**	**03/31/08**	**06/30/08**	**09/30/08**	**12/31/08**	**03/31/09**	**06/30/09**	**09/30/09**
ESSA Bancorp, Inc.	100.00	93.80	94.65	95.50	99.75	106.62	118.72	121.03	114.38	117.83	114.32
SNL Thrift Index	100.00	98.24	91.79	64.44	61.45	50.83	47.28	41.01	34.37	34.44	36.21
Russell 2000	100.00	103.10	99.91	95.34	85.90	86.41	85.44	63.13	53.69	64.79	77.29

Source : SNL Financial LC, Charlottesville, NC

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On May 27, 2008, the Board of Directors approved a stock repurchase program and authorized the repurchase of up to 15% of the Company s outstanding shares of common stock. In June, 2009 the Company announced the completion of its 15% repurchase program after having purchased 2,547,135 shares at a weighted average cost of $13.14. Also in June, 2009 the Company announced a second repurchase program to purchase up to an additional 10% of its outstanding stock. Stock repurchases will be made from time to time and may be effected through open market purchases, block trades and in privately negotiated transactions. Repurchased stock will be held as treasury stock and will be available for general corporate purposes. No time limit was placed on the duration of the share repurchase program. As of September 30, 2009, 112,000 shares have been repurchased as described in the following table:

Company Purchases of Common Stock

Period	Total number of shares purchased	Average price paid per share	Total number of shares purchased as part of publicly announced plans or programs	Maximum number of shares that may yet be purchased under the plans or programs
July 1, 2009 through July 31, 2009				1,499,062
August 1, 2009 through August 31, 2009	53,300	13.40	53,300	1,445,762
September 1, 2009 through September 30, 2009	58,700	12.73	58,700	1,387,062
Total	112,000	13.05	112,000	

Item 6. Selected Financial Data

The following information is derived from the audited consolidated financial statements of ESSA Bancorp, Inc. For additional information, reference is made to Management s Discussion and Analysis of Financial Condition and Results of Operations and the Consolidated Financial Statements of ESSA Bancorp, Inc. and related notes included elsewhere in this Annual Report.

	At September 30,				
	2009	2008	2007	2006	2005
	(In thousands)				
Selected Financial Condition Data:					
Total assets	$ 1,042,119	$ 993,482	$ 910,415	$ 725,796	$ 656,066
Cash and cash equivalents	18,593	12,614	16,779	12,730	20,290
Investment securities:					
Available for sale	217,566	204,078	205,267	89,122	62,506
Held to maturity	6,709	11,857	17,130	19,715	21,505
Loans, net	733,580	706,890	619,845	556,677	508,981
Federal Home Loan Bank stock	20,727	19,188	16,453	13,675	11,916
Premises and equipment	10,620	10,662	11,277	11,447	11,560
Bank owned life insurance	15,072	14,516	13,941	13,376	12,864
Deposits	408,855	370,529	384,716	402,153	374,759
Borrowed funds	438,598	412,757	313,927	259,299	221,479
Equity	185,506	200,086	204,692	58,337	54,371

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	For the Year Ended September 30, 2009	2008	2007 (In thousands)	2006	2005
Selected Data:					
Interest income	$ 52,733	$ 52,065	$ 45,510	$ 36,451	$ 31,919
Interest expense	23,739	25,642	23,805	19,217	14,323
Net interest income	28,994	26,423	21,705	17,234	17,596
Provision for loan losses	1,500	900	360	300	550
Net interest income after provision for loan losses	27,494	25,523	21,345	16,934	17,046
Non-interest income	5,728	4,803	5,496	5,518	5,281
Non-interest expense	24,113	21,181	31,185	16,685	16,493
Income (loss) before income tax expense	9,109	9,145	(4,344)	5,767	5,834
Income tax expense	2,553	3,068	782	1,813	1,383
Net income (loss)	$ 6,556	$ 6,077	$ (5,126)	$ 3,954	$ 4,451
Earnings (loss) per share [1]					
Basic	$ 0.47	$ 0.39	$ (0.47)	$ N/A	$ N/A
Diluted	$ 0.47	$ 0.38	$ (0.47)	$ N/A	$ N/A

[1] Earnings per share for 2007 are calculated for the period beginning with the Company s date of conversion of April 3, 2007.

	At or For the Year Ended September 30, 2009	2008	2007	2006	2005
Selected Financial Ratios and Other Data:					
Performance Ratios:					
Return on average assets	0.64%	0.63%	(0.62)%	0.58%	0.72%
Return on average equity	3.42%	2.92%	(3.88)%	6.96%	8.42%
Interest rate spread (1)	2.40%	2.09%	2.18%	2.46%	2.85%
Net interest margin (2)	2.93%	2.88%	2.78%	2.70%	3.04%
Efficiency ratio (3)	69.45%	67.83%	116.18%	73.33%	72.09%
Noninterest expense to average total assets	2.34%	2.21%	3.78%	2.45%	2.67%
Average interest-earning assets to average interest-bearing liabilities	123.00%	128.60%	120.21%	108.00%	107.69%
Asset Quality Ratios:					
Non-performing assets as a percent of total assets	0.74%	0.40%	0.06%	0.07%	0.10%
Non-performing loans as a percent of total loans	0.70%	0.55%	0.09%	0.08%	0.12%
Allowance for loan losses as a percent of non-performing loans	112.82%	124.81%	757.83%	809.87%	588.93%
Allowance for loan losses as a percent of total loans	0.79%	0.69%	0.67%	0.69%	0.70%
Capital Ratios:					
Total risk-based capital (to risk weighted assets)	31.00%	30.30%	32.84%	15.77%	15.55%
Tier 1 risk-based capital (to risk weighted assets)	29.86%	29.42%	31.88%	14.79%	14.59%
Tangible capital (to tangible assets)	15.17%	15.50%	16.61%	8.06%	8.30%
Tier 1 leverage (core) capital (to adjusted tangible assets)	15.17%	15.50%	16.61%	8.06%	8.30%
Average equity to average total assets	18.59%	21.77%	15.98%	8.36%	8.55%
Other Data:					
Number of full service offices	13	13	13	12	12

(1) The interest rate spread represents the difference between the weighted-average yield on a fully tax equivalent basis on interest-earning assets and the weighted-average cost of interest-bearing liabilities for the year.
(2) The net interest margin represents net interest income on a fully tax equivalent basis as a percent of average interest-earning assets for the year.
(3) The efficiency ratio represents non-interest expense divided by the sum of net interest income and non-interest income.

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Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations
Business Strategy

Our business strategy is to grow and improve our profitability by:

- Increasing customer relationships through the offering of excellent service and the distribution of that service through effective delivery systems;
- Continuing to transform into a full service community bank by meeting the financial services needs of our customers;
- Continuing to develop into a high performing financial institution, in part by increasing interest revenue and fee income;
- Remaining within our risk management parameters; and
- Employing affordable technology to increase profitability and improve customer service.

We intend to continue to pursue our business strategy, subject to changes necessitated by future market conditions and other factors. We also intend to focus on the following:

- ***Increasing customer relationships through a continued commitment to service and enhancing products and delivery systems.*** We will continue to increase customer relationships by focusing on customer satisfaction with regard to service, products, systems and operations. We have upgraded and expanded certain of our facilities, including our corporate center, to provide additional capacity to manage future growth and expand our delivery systems.
- ***Continuing to transform into a full-service community bank.*** We continue to transform from a traditional savings association into a full-service community bank. During the last several years, we have begun to offer a wide variety of commercial loans and deposits, as well as trust and brokerage services.
- ***Continuing to develop into a high performing financial institution.*** We will continue to enhance profitability by focusing on increasing non-interest income as well as increasing commercial products, including commercial real estate lending, which often have a higher profit margin than more traditional products. We also will pursue lower-cost commercial deposits as part of this strategy.
- ***Remaining within our risk management parameters.*** We place significant emphasis on risk management and compliance training for all of our directors, officers and employees. We focus on establishing regulatory compliance programs to determine the degree of such compliance and to maintain the trust of our customers and community.
- ***Employing cost-effective technology to increase profitability and improve customer service.*** We will continue to upgrade our technology in an efficient manner. We have implemented new software for marketing purposes and have upgraded both our internal and external communication systems.

Continuing our emphasis on commercial real estate lending to improve our overall performance. We intend to continue to emphasize the origination of higher interest rate margin commercial real estate loans as market conditions, regulations and other factors permit. We have expanded our commercial banking capabilities by adding experienced commercial bankers, and enhancing our direct marketing efforts to local businesses.

Expanding our banking franchise through branching and acquisitions. We will attempt to use the net proceeds from the offering, as well as our new stock holding company structure, to expand our market footprint through *de novo* branching as well as through acquisitions of banks, savings institutions and other financial service providers in our primary market area. We will also consider establishing *de novo* branches or acquiring financial institutions in contiguous counties. We have begun construction on a new branch in Monroe County. We expect this branch to open in February, 2010. We have also signed leases to establish two supermarket branches in Northampton County and one supermarket branch in Lehigh County. We expect these branches to open during our third fiscal quarter. We will continue to review and assess locations for new branches both within Monroe County and the contiguous counties around Monroe. There can be no assurance that we will be able to consummate any acquisitions or establish any additional new branches. We may explore acquisition opportunities involving other banks and thrifts, and possibly financial service companies, when and as they arise, as a means of supplementing internal growth, filling gaps in our current geographic market area and expanding our customer base, product lines and internal capabilities, although we have no current plans, arrangements or understandings to make any acquisitions.

Maintaining the quality of our loan portfolio. Maintaining the quality of our loan portfolio is a key factor in managing our growth. We will continue to use customary risk management techniques, such as independent internal and external loan reviews, risk-focused portfolio credit analysis and field inspections of collateral in overseeing the performance of our loan portfolio.

Critical Accounting Policies

We consider accounting policies that require management to exercise significant judgment or discretion or make significant assumptions that have, or could have, a material impact on the carrying value of certain assets or on income, to be critical accounting policies. We consider the following to be our critical accounting policies:

Allowance for Loan Losses. The allowance for loan losses is the estimated amount considered necessary to cover credit losses inherent in the loan portfolio at the balance sheet date. The allowance is established through the provision for loan losses which is charged against income. In determining the allowance for loan losses, management makes significant estimates and has identified this policy as one of our most critical. The methodology for determining the allowance for loan losses is considered a critical accounting policy by management due to the high degree of judgment involved, the subjectivity of the assumptions utilized and the potential for changes in the economic environment that could result in changes to the amount of the recorded allowance for loan losses.

As a substantial amount of our loan portfolio is collateralized by real estate, appraisals of the underlying value of property securing loans and discounted cash flow valuations of properties are critical in determining the amount of the allowance required for specific loans. Assumptions for appraisals and discounted cash flow valuations are instrumental in determining the value of properties. Overly optimistic assumptions or negative changes to assumptions could significantly impact the valuation of a property securing a loan and the related allowance determined. The assumptions supporting such appraisals and discounted cash flow valuations are carefully reviewed by management to determine that the resulting values reasonably reflect amounts realizable on the related loans.

Management performs a quarterly evaluation of the adequacy of the allowance for loan losses. Consideration is given to a variety of factors in establishing this estimate including, but not limited to, current economic conditions, delinquency statistics, geographic and industry concentrations, the adequacy of the underlying collateral, the financial strength of the borrower, results of internal and external loan reviews and other relevant factors. This evaluation is inherently subjective, as it requires material estimates that may be susceptible to significant revision based on changes in economic and real estate market conditions.

The analysis of the allowance for loan losses has two components: specific and general allocations. Specific allocations are made for loans that are determined to be impaired. Impairment is measured by determining the present value of expected future cash flows or, for collateral-dependent loans, the fair value of the collateral adjusted for market conditions and selling expenses. The general allocation is determined by segregating the remaining loans by type of loan, risk weighting (if applicable) and payment history. We also analyze historical loss experience, delinquency trends, general economic conditions and geographic and industry concentrations. This analysis establishes factors that are applied to the loan groups to determine the amount of the general allocations. Actual loan losses may be significantly more than the allowance for loan losses we have established which could have a material negative effect on our financial results.

Other-than-Temporary Investment Security Impairment. Securities are evaluated periodically to determine whether a decline in their value is other-than-temporary. Management utilizes criteria such as the magnitude and duration of the decline, in addition to the reasons underlying the decline, to determine whether the loss in value is other-than-temporary. The term other-than-temporary is not intended to indicate that the decline is permanent, but indicates that the prospect for a near-term recovery of value is not necessarily favorable, or that there is a lack of evidence to support a realizable value equal to or greater than the carrying value of the investment. Once a decline in value is determined to be other-than-temporary, the value of the security is reduced and a corresponding charge to earnings is recognized.

Deferred Income Taxes. We use the asset and liability method of accounting for income taxes. Under this method, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. If current available information raises doubt as to the realization of the deferred tax assets, a valuation allowance is established. We consider the determination of this valuation allowance to be a critical accounting policy because of the need to exercise significant judgment in evaluating the amount and timing of recognition of deferred tax liabilities and assets, including projections of future taxable income. These judgments and estimates are reviewed on a continual basis as regulatory and business factors change. A valuation allowance for deferred tax assets may be required if the amount of taxes recoverable through loss carryback declines, or if we project lower levels of future taxable income. Such a valuation allowance would be established through a charge to income tax expense which would adversely affect our operating results.

Comparison of Financial Condition at September 30, 2009 and September 30, 2008

Total Assets. Total assets increased $48.6 million, or 4.9%, to $1.04 billion at September 30, 2009, compared to $993.5 million at September 30, 2008. This increase was primarily due to increases in net loans receivable, interest-bearing deposits with other banks and investment securities available for sale offset in part by decreases in cash and due from banks and investment securities held to maturity.

Cash and Due from Banks. Cash and due from banks decreased $1.3 million or 15.3% to $7.1 million at September 30, 2009 from $8.4 million at September 30, 2008. The primary reason for this decrease was a decrease in the Company s cash balance at the Federal Reserve Bank of Philadelphia which was partially offset by increases in the Company s cash on hand at the Bank s branch locations. Both of these cash balances fluctuate based on the customer trends and demands within our branch network.

Interest-Bearing Deposits with Other Institutions. Interest-bearing deposits with other institutions increased $7.3 million, or 171.5%, to $11.5 million at September 30, 2009 from $4.2 million at September 30, 2008. The primary reason for the increase was an increase in the Company s interest bearing demand deposit account at the FHLBank Pittsburgh of $7.3 million.

Investment Securities Available for Sale. Investment securities available for sale increased $13.5 million, or 6.6% to $217.6 million at September 30, 2009 from $204.1 million at September 30, 2008. The increase was due primarily to an increase of $40.3 million in the Company s portfolio of mortgage-backed securities issued by United States sponsored agencies or entities offset in part by a $27.1 million decrease in the Company s portfolio of United States government agency securities. The growth in the mortgage-backed securities was due to the reinvestment of the proceeds from United States government agency security maturities, the investment of approximately $20.0 million in mortgage-backed securities issued by United States government sponsored agencies or entities as part of a leverage strategy to take advantage of the steepening yield curve, and the partial reinvestment of the proceeds from the sale of $26.4 million of thirty year, fixed rate mortgage loans.

Investment Securities Held to Maturity. Investment securities held to maturity decreased $5.1 million or 43.4% to $6.7 million at September 30, 2009 from $11.9 million at September 30, 2008. The primary reasons for this decrease were the maturities of U.S. Government Agency Securities and repayments received on mortgage-backed securities issued by U.S. Government Agencies.

Net Loans. Net loans increased $26.7 million, or 3.8%, to $733.6 million at September 30, 2009 from $706.9 million at September 30, 2008. Loan growth was primarily attributable to growth in several product categories as a result of our continued marketing efforts and a decrease in the number of non-financial institution competitors. One-to four-family residential mortgages increased by $31.8 million to $603.8 million at September 30, 2009 from $572.0 million at September 30, 2008. For the same period, commercial real estate loans decreased by $1.5 million to $68.0 million at September 30, 2009 from $69.5 million at September 30, 2008, construction loans outstanding decreased by $6.5 to $1.7 million at September 30, 2009 from $8.3 million at September 30, 2008, and commercial loans increased by $4.5 million to $16.5 million at September 30, 2009 from $12.0 million at September 30, 2008.

Federal Home Loan Bank Stock. Federal Home Loan Bank stock increased $1.5 million, or 3.8%, to $20.7 million at September 30, 2009 from $19.2 million at September 30, 2008. The Bank is a member of the Federal Home Loan Bank System. As a member, the Bank maintains an investment in the capital stock of the FHLBank Pittsburgh in an amount not less than 70 basis points of the outstanding unused FHLB borrowing capacity or $^{1}/_{20}$ of its outstanding FHLB borrowings, whichever is greater, as calculated throughout the year. FHLBank Pittsburgh borrowings outstanding at September 30, 2009 were $343.6 million compared to borrowings of $367.8 million at September 30, 2008.

Deposits. Deposits increased by $38.3 million, or 10.3%, to $408.9 million at September 30, 2009 from $370.5 million at September 30, 2008. The increase in deposits was primarily due to increases in money market accounts of $34.5 million, savings and club accounts of $4.9 million and brokered certificates of deposit of $11.0 million offset in part by a decrease in retail certificates of deposit of $11.3 million. The increase in brokered certificates was the result of the Company s decision to purchase certificates based on the cost of those certificates compared to other available funding sources. Money market accounts increased in part in response to rate promotions for that product along with customers reinvesting proceeds of certificate of deposit maturities. At September 30, 2009, the Company had $22.0 million of brokered certificates of deposit outstanding.

Borrowed Funds. Borrowed funds, short term and other, increased $25.8 million or 6.3% to $438.6 million at September 30, 2009 from $412.8 million at September 30, 2008. Included in borrowed funds at September 30, 2009 were $65.0 million of repurchase agreements with various financial institution third parties. Except for these borrowings all borrowed funds are from the FHLBank Pittsburgh or the Federal Reserve Bank of Philadelphia. The increase in borrowed funds was primarily due to the need to fund additional loan growth and to purchase investment securities and certificates of deposit.

Stockholders Equity. Stockholders equity decreased by $14.6 million, or 7.3% to $185.5 million at September 30, 2009 from $200.1 million at September 30, 2008. This decrease was primarily the result of stock repurchases of $24.9 million funded by proceeds of investment maturities and the payment of cash dividends of $2.4 million which were partially offset by net income of $6.6 million for the year ending September 30, 2009 and an increase in the unrealized gains, net of taxes on available for sale securities of $4.4 million at September 30, 2009 compared to September 30, 2008.

Comparison of Operating Results for the Years Ended September 30, 2009 and September 30, 2008

Net Income. Net income increased $479,000 to $6.6 million for the fiscal year ended September 3